REPORT BY THE

# Comptroller General

OF THE UNITED STATES

## Agencies Need Better Guidance For Choosing Among Contracts, Grants, And Cooperative Agreements

COMPLETED

101

The Federal Grant and Cooperative Agreement Act distinguishes Federal procurement from Federal assistance relationships and further distinguishes between grant and cooperative agreement types of Federal assistance. However, Federal agencies do not always select the appropriate instrument because of vague OMB guidance and less-than aggressive implementation by the agencies. As a result, the Federal interest may not be adequately protected in some procurement situations. Further, development of a more orderly and less burdensome Federal assistance system anticipated by the Congress has been impeded.

GAO recommends that the Office of Management and Budget clarify its guidance, more actively direct and oversee Federal agencies' implementation of the act, and establish clear differences among contracts, grants, and cooperative agreements. GAO also recommends that the Congress extend OMB's authority to except individual programs or transactions from the act's provisions.

GGD-81-88
SEPTEMBER 4, 1981

I

Request for copies of GAO reports should be sent to:

U.S. General Accounting Office
Document Handling and Information
Services Facility
P.O. Box 6015
Gaithersburg, Md. 20760

Telephone (202) 275-6241

The first five copies of individual reports are free of charge. Additional copies of bound audit reports are $3.25 each. Additional copies of unbound report (i.e., letter reports) and most other publications are $1.00 each. There will be a 25% discount on all orders for 100 or more copies mailed to a single address. Sales orders must be prepaid on a cash, check, or money order basis. Check should be made out to the "Superintendent of Documents".

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

B-196872

The Honorable Lawton Chiles
United States Senate

Dear Senator Chiles:

As you requested in your August 1, 1978, letter, we monitored the implementation of the Federal Grant and Cooperative Agreement Act of 1977. This report discusses Federal agencies' efforts to implement the act and actions we believe are necessary to accomplish the act's objectives.

As arranged with your office, we are sending copies of this report to interested members and committees of the Congress; the Assistant to the President for Intergovernmental Relations; the Director, Office of Management and Budget; the heads of Federal agencies discussed in the report; and other interested parties.

Sincerely yours,

Milton J. Socolar

Acting Comptroller General
of the United States

III

REPORT BY THE COMPTROLLER
GENERAL OF THE UNITED STATES

# AGENCIES NEED BETTER GUIDANCE FOR CHOOSING AMONG CONTRACTS, GRANTS, AND COOPERATIVE AGREEMENTS

## D I G E S T


The purposes of the Federal Grant and Cooperative Agreement Act of 1977 have not been fully achieved.

The major purposes of the act are to distinguish the types of relationships the Federal Government enters into with recipients of Federal awards and to bring about uniformity in the selection and use of contracts, grants, and cooperative agreements.

The Congress passed the act primarily because failure of Federal agencies to distinguish among procurement and various assistance relationships had led to the inappropriate use of grants to avoid the requirements of the procurement system, and to unnecessary red tape and administrative requirements in grants. Although the act was intended in part to curb the misuse of assistance instruments in procurement situations, Federal officials sometimes misinterpret the act and select assistance instruments where GAO believes procurement contracts are appropriate. As a result, Federal procurement requirements designed to protect the Federal interest and ensure competition may not be applied.

The Congress also intended to establish a systematic approach for distinguishing among assistance relationships based on the degree of Federal involvement with the recipient. However, due to vague guidance and a less-than-aggressive effort to implement the act by many agencies, assistance relationships are often not reviewed to ensure that

--Federal involvement is consistent with congressional intent and the agency's experience with a recipient,

--the legal instrument used matches the intended relationship,

--the terms and conditions of the instrument selected are the minimum necessary to assure that Federal funds are spent efficiently and for authorized purposes, and

--these terms and conditions clearly establish the roles and responsibilities of the Federal Government and the recipient.

To further the purposes of the act, OMB needs to clarify its guidelines and promote more aggressive implementation by Federal agencies. OMB should ensure that meaningful differences among contracts, grants, and cooperative agreements are established. Unless steps are taken to establish clear differences among these instruments, it is unlikely that the act will fully achieve its purposes.

The Chairman of the former Subcommittee on Federal Spending Practices and Open Government, Senate Committee on Governmental Affairs, asked GAO to monitor implementation of the Federal Grant and Cooperative Agreement Act. This report discusses the extent to which Federal agencies have implemented the act, whether this implementation has been proper, and what Government-wide issues resulted from implementation.

## AGENCIES STILL USE GRANTS AND COOPERATIVE AGREEMENTS INSTEAD OF CONTRACTS

Federal agencies' misunderstandings of key provisions of the act and OMB's guidance have resulted in some circumvention of the procurement system and also to a potential unwarranted expansion of their authority to enter into assistance arrangements. (See p. 7.) Contributing to this problem is the gradual erosion of the differences between procurement and assistance procedures.

The act requires Federal agencies to use a type of procurement contract when the principal purpose of the relationship with a recipient is to acquire something for the direct benefit or use of the Federal Government. An assistance relationship, on the other hand, occurs when the principal purpose of the relationship is to

transfer money, property, or anything of value to a recipient to accomplish a public purpose of support or stimulation.

Some Federal agencies will not use a procurement contract unless the Federal Government "benefits" more than other parties. This interpretation of the direct benefit clause gives rise to the use of assistance awards rather than contracts for such things as the production of a Federal agency program guidance manual or the use of an intermediary to perform accounting and bill payment services for a Federal agency. GAO believes these practices are questionable and reflect a misunderstanding of the act. (See p. 9.)

GAO also noted cases in which officials interpreted the act as giving them broad new independent authority to enter into assistance relationships when no such authority previously existed. GAO believes the Congress intended to correct inconsistencies in prior terminology used to characterize agency/recipient relationships but did not intend to authorize agencies to use grants, cooperative agreements, or contracts irrespective of the basic relationships authorized by substantive program legislation. (See p. 15.)

## NEED FOR BETTER DEFINITIONS OF GRANTS AND COOPERATIVE AGREEMENTS

Federal agencies are having problems determining when to use a cooperative agreement or a grant in their assistance awards. Their problems center on determining whether or not substantial Federal involvement is anticipated in recipient activities. When substantial involvement is anticipated, cooperative agreements are to be used. Conversely, grants are for situations in which no substantial Federal involvement is anticipated.

Although a good first step, OMB's guidelines do not adequately define these levels of involvement. (See p. 22.) Further, OMB management circulars setting forth Government-wide requirements and operating procedures for assistance programs apply equally to grants and cooperative agreements. (See p. 54.)

Until meaningful distinctions between grants and cooperative agreements are developed, the act will have little practical effect in rationalizing the Federal assistance system. GAO recognizes the difficulty in developing Government-wide guidelines and offers an interim approach to promote more uniformity in the selection and use of these instruments. (See p. 27.)

GAO's suggested approach involves having agencies identify what is normal involvement for their programs and then base their grant and cooperative agreement distinctions on the extent to which they are more involved than normal with individual recipients. The fact that a recipient is treated differently, i.e., subjected to more controls or agency collaboration, and has less discretion than the normal program recipient suggests that the agency is substantially involved and a cooperative agreement is appropriate.

GAO recognizes the interim approach will not yield total uniformity. For example, under this approach similar relationships entered into by two agencies might be called grants by one and cooperative agreements by the other. However, the approach will provide a more structured basis for agencies' decisions and will provide the operating data needed to start developing uniform Government-wide standards.

## IMPLEMENTATION EFFORTS NEED IMPROVEMENT

The steps taken by OMB and Federal agencies to implement the act were not totally effective. Many Federal officials did not know of the act or had inadequate information to apply it. Other Federal officials resisted applying the act because they believed a change in terminology for their assistance instruments would be detrimental to their existing recipient relationships. (See p. 38.)

If the objectives of the act are to be attained, OMB and Federal agencies need to place increased emphasis on the administration of the act. (See pp. 42 to 47.) Both need to establish better coordination and oversight mechanisms to ensure that officials' awareness of the act is increased,

different practices and procedures are identified and resolved, and policies conform with the objectives of the act.

Because the act has yet to be applied to many programs, GAO also believes OMB's authority to except individual programs or transactions from the act's coverage should be renewed. Until it expired in March 1981, the authority was useful and OMB exercised it judiciously. (See p. 47.)

RECOMMENDATION TO THE CONGRESS

To accommodate potential unanticipated consequences from the act's use and to facilitate consistent implementation, the Congress should renew OMB's authority to except individual programs or transactions from the act's provisions. (See p. 49.)

RECOMMENDATIONS TO THE DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET

The Director, OMB, should undertake specific actions to improve the implementation of the act. These actions involve

--improving OMB guidance on how agencies should choose between types of procurement contracts and assistance instruments and on how to choose between grants and cooperative agreements (see pp. 31 and 32);

--increasing monitoring and administration of the act by OMB and Federal agencies (see p. 49); and

--establishing clear operational differences among contracts, grants, and cooperative agreements (see p. 61).

AGENCY COMMENTS

GAO received comments on a draft of this report from OMB; the Departments of the Interior, Energy, Transportation, Justice, and Housing and Urban Development; the Environmental Protection Agency; ACTION; and the Inspector General of the Department of Health and Human Services. (See app. I through IX.)

Tear Sheet

OMB agreed with GAO's interpretation of key provisions of the act and generally agreed with GAO's recommendations. OMB plans to:

--Improve its guidance consistent with most of our recommendations on how agencies should choose between types of procurement contracts and assistance instruments (see p. 32).

--Facilitate better monitoring and administration of the act through a broader effort to improve the management of all generally applicable assistance policies (see p. 50).

--Consider establishing clear operational differences among contracts, grants, and cooperative agreements (see p. 62).

The other agencies basically viewed the report as thorough and useful. The Departments of the Interior, Energy, and Justice agreed with GAO's recommendations, but they and the other agencies expressed individual reservations. (See pp. 32, 50, and 62.)

# Contents


| | | Page |
|---|---|---|
| DIGEST | | i |
| CHAPTER | | |
| 1 | INTRODUCTION | 1 |
| | The Federal Grant and Cooperative Agreement Act | 1 |
| | Objectives, scope, and methodology | 5 |
| 2 | INCORRECT INSTRUMENTS CAN BE CHOSEN BECAUSE GUIDANCE IS VAGUE | 7 |
| | Clearer terms and procedures needed to distinguish between procurement and assistance | 7 |
| | Need to improve cooperative agreement guidance | 22 |
| | Conclusions | 30 |
| | Recommendations to the Director, OMB | 31 |
| | Agency comments and our evaluation | 32 |
| 3 | STRONGER OMB AND AGENCY MANAGEMENT EFFORTS NEEDED TO IMPLEMENT THE ACT | 37 |
| | The criteria of the act are frequently not being used | 37 |
| | Agencies need to establish better implementation systems | 42 |
| | OMB oversight of agency implementation of the act should be strengthened | 45 |
| | OMB's authority to except programs was beneficial and should be renewed | 47 |
| | Conclusions | 48 |
| | Recommendation to the Congress | 49 |
| | Recommendations to the Director, OMB | 49 |
| | Agency comments and our evaluation | 50 |
| 4 | NEED TO DEVELOP DIFFERENCES IN OPERATING PROCEDURES FOR GRANTS, COOPERATIVE AGREEMENTS, AND CONTRACTS | 51 |
| | Differences between procurement and assistance procedures appear to be eroding | 51 |
| | Differences between grants and cooperative agreements need to be established | 54 |

Conclusions 61
Recommendation to the Director, OMB 61
Agency comments and our evaluation 62

APPENDIX

I Letter received July 2, 1981, from the Associate Director for Management, Office of Management and Budget 63

II Letter dated June 26, 1981, from the Deputy Assistant Secretary, Policy, Budget, and Administration, Department of the Interior 68

III Letter dated June 25, 1981, from the Assistant Secretary, Management and Administration, Department of Energy 69

IV Letter dated June 25, 1981, from the Assistant Secretary for Administration, Department of Transportation 71

V Letter dated June 18, 1981, from the Assistant Attorney General for Administration, Department of Justice 76

VI Letter dated June 18, 1981, from the Acting Deputy Assistant Secretary for Administration, Department of Housing and Urban Development 80

VII Letter dated June 30, 1981, from the Acting Assistant Administrator for Planning and Management, Environmental Protection Agency 82

VIII Letter received June 26, 1981, from the Director, ACTION 86

IX Letter dated June 24, 1981, from the Inspector General, Department of Health and Human Services 88

ABBREVIATIONS

CDBG Community Development Block Grant

CSA Community Services Administration

DOT Department of Transportation

EDA Economic Development Administration

EPA Environmental Protection Agency

| | |
|---|---|
| GAO | General Accounting Office |
| HHS | Health and Human Services |
| HUD | Housing and Urban Development |
| NASA | National Aeronautics and Space Administration |
| NIC | National Institute of Corrections |
| NSF | National Science Foundation |
| OFPP | Office of Federal Procurement Policy |
| OMB | Office of Management and Budget |
| REA | Rural Electrification Administration |
| SSA | Social Security Administration |
| UMTA | Urban Mass Transportation Administration |

# CHAPTER 1

## INTRODUCTION

In recent years, the size and scope of the Federal domestic assistance system has grown dramatically. Federal aid to State and local governments has almost tripled, growing from $24 billion in 1970 to about $90 billion for fiscal year 1980. This growth in financial assistance has been accompanied by similar increases in the number of programs awarding funds and the attendant Federal administrative requirements. In addition to providing financial assistance, the Federal Government is also heavily involved in procurement of goods and services for its own use. Together, this spending for activities such as research, construction, flood control, transportation, community development, health care, and social services comprises a significant part of the national budget.

Federal agencies use a wide variety of agreements in their procurement and assistance relationships. These agreements include (1) procurement contracts for acquiring goods and services for Federal Government use or benefit, and (2) assistance agreements, like grants, cooperative agreements, loans, and subsidies, with non-Federal parties to support or stimulate activities deemed in the national interest. This report is concerned with procurement contracts and the grant and cooperative agreement types of Federal assistance.

### THE FEDERAL GRANT AND COOPERATIVE AGREEMENT ACT

Major efforts have been underway over the last decade to reform both the procurement and assistance systems. The Commission on Government Procurement (Procurement Commission), established by the Congress in 1969, studied and made numerous recommendations for improving agency procurement procedures. Many of these recommendations have been adopted by the executive branch and the Congress. Several other efforts to reform assistance programs have also been undertaken by the Congress and the executive branch.

One reform effort was common to both the procurement and assistance systems. The Congress sought to bring order to the awarding of financial assistance and the procurement of goods and services through the Federal Grant and Cooperative Agreement Act of 1977. Prior to this act, no uniform statutory guidance existed which expressed congressional policy on the use of grants and contracts. As a result, Federal agencies often improperly selected grants and contracts interchangeably without significant regard for the type of relationship being established.

In some instances, Federal agencies have administered assistance agreements as though they were contracts. Generally, this has occurred where Federal officials believed certain controls were necessary to protect the Federal interest, even though the relationship was one of assistance. Grants also were sometimes used to avoid competition and other requirements of the procurement system.

The improper use of contracts and grants or confusion between procurement and assistance relationships leads to inadequate protection of Federal interests and to unnecessarily stringent requirements on recipients of assistance awards. Because their premises differ, contracts and grants have different requirements and consequences. Federal procurement regulations and an extensive body of common law are applied to contracts. The Federal procurement regulations have extensive and detailed procedures for competition and the overall process of awarding contracts. Contracts are also subject to other Federal requirements, such as preferences given socially and economically disadvantaged small businesses, which are either not applied to assistance awards or are merely encouraged. Assistance instruments, although often considered to be a form of contract, have not generally been held to be subject to the Federal procurement regulations and the extensive body of contract law. A set of guidelines for assistance is evolving, and the body of law relating to Federal assistance is growing.

As indicated above, the Procurement Commission studied and recommended ways to improve the Federal procurement process. Because of the importance of Federal grant activities and the uncertainty about how grant and procurement relationships differ, the Commission also conducted a limited review of Federal assistance programs. In its 1972 report the Commission concluded that the failure to clearly distinguish between procurement and assistance relationships led to the use of grants to avoid the requirements of the procurement process, and to unnecessary red tape and administrative requirements in grants. The Commission also found that unlike procurement programs, assistance programs operated without the benefits of a clear and comprehensive system of guidance. The Commission recommended that the Congress enact legislation to distinguish procurement and assistance relationships and require a study of assistance programs be conducted to determine the feasibility of developing a comprehensive system of guidance.

The Congress passed the Federal Grant and Cooperative Agreement Act primarily as a result of the Commission's recommendation. The Congress believed that the legal agreement used for each transaction should communicate the roles and responsibilities of both the Federal Government and the recipient of the Federal award. The Congress further believed that the need to apply the criteria of the act to choose a specific legal instrument would force Federal

administrators to carefully review proposed awards and identify unnecessary administrative requirements affecting the administration of those awards.

Other concerns of the Congress, Federal, State, and local governments, and of private nonprofit and profit firms also contributed to the act's passage and basic form. The Congress intended to (1) increase competition in assistance awards, (2) reduce the complexity and resulting confusion and inefficiency it saw in the assistance system, and (3) reduce the inappropriate use of grants to avoid the controls and procedures of the procurement system. State and local officials and nonprofit organizations who receive Federal awards were also concerned with excessive Federal involvement in the administration of assistance programs, and saw the act as a possible way to increase the discretion of recipients to manage the programs. Concerns expressed by profitmaking firms that they were not allowed to compete for grants were also addressed to some extent by the act. Such firms were not explicitly excluded from eligibility for assistance awards, but the issue was to be a subject for further study.

## What the act did and did not do

The act provides the criteria Federal agencies are to use to uniformly and consistently distinguish procurement relationships from assistance relationships. It mandates that Federal agencies use a type of procurement contract as the legal instrument for acquisitions of property or services for the direct benefit or use of the Federal Government. Grants or cooperative agreements are the legal instruments for transfering money, property, services, or anything of value to recipients to accomplish a public purpose of support or stimulation. Grants are to be used when no substantial Federal agency involvement occurs during recipient performance of the activity. Cooperative agreements are required when substantial involvement is anticipated. Federal agencies were required to apply the criteria of the act by February 3, 1979.

During congressional deliberations, Federal officials expressed concern that the criteria of the act were somewhat vague and that unintended consequences could result from use of the act. In response to these concerns the Congress gave OMB authority to except transactions and programs. This authority expired in March 1981. The Congress expected that experiences of Federal agencies in applying the criteria of the act would provide evidence for revising and improving the criteria of the act.

The act does not cover all possible relationships that may exist between Federal agencies and others. For example, it does not cover any agreement under which Federal cash assistance is

provided directly to individuals, or a subsidy, loan, loan guarantee, or insurance is provided.

The Office of Management and Budget was required by the act to conduct a study of Federal assistance programs and provide a report to the Congress by early February 1980. The study was to focus on developing a better understanding of alternative means to implement Federal assistance programs. Based in part on the experience Federal agencies gained in the use of the criteria of the act, the study also was to determine if it was feasible to develop a comprehensive system of guidance for Federal assistance programs, perhaps analogous to Federal procurement regulations. Further, OMB was charged with recommending changes to the act that might be necessary to implement its findings.

## Office of Management and Budget guidelines implementing the act

As authorized by the act, the Office of Management and Budget issued guidelines to Federal agencies on August 18, 1978, to promote consistent and efficient use of contracts, grants, and cooperative agreements. The guidance includes specific instructions to help agencies make decisions on the use of these instruments. It describes how OMB interprets several provisions of the act and how OMB will administer agencies' requests for exceptions. The guidance further describes how agencies should apply existing OMB administrative standards to grants and cooperative agreements.

The guidance provides OMB's response to many agency requests for clarification on how to select among the authorized instruments. It also requires Federal agencies to insure that general decisions are either made or reviewed at a policy level on whether a program is principally procurement or assistance and whether substantial Federal involvement will occur in assistance programs. Agencies are required to document how these decisions are made so that data will be available to measure the effects of implementation of the act and so that amendments to the act can be drafted if necessary.

The guidance also emphasizes that the act's objectives are consistent with other Presidential initiatives to improve management of Federal assistance, and states that the act provides an important opportunity to review, improve, and simplify Federal assistance programs.

## OBJECTIVES, SCOPE, AND METHODOLOGY

In an August 1, 1978, letter, the Chairman, Subcommittee on Federal Spending Practices and Open Government 1/, Senate Committee on Governmental Affairs, asked us to monitor the implementation of the Federal Grant and Cooperative Agreement Act. We were asked to determine to what extent Federal agencies have implemented the act, whether this implementation has been proper, and what Government-wide issues resulted from implementation.

In order to accomplish these objectives, we concentrated on efforts by OMB and the executive agencies to apply the act's criteria when selecting grants, cooperative agreements, or contracts. In addition, we monitored OMB's study of Federal assistance programs and obtained information on issues relevant to the effective implementation of the act. To determine the intent of the act and circumstances leading to its passage, we interviewed Federal executive and congressional officials who were active in the events and deliberations leading to the act and reviewed the act's legislative history.

To determine the extent of implementation of the act we administered a questionnaire to a Government-wide, randomly selected and stratified sample of Federal headquarters officials. We completed telephone interviews with responsible headquarters officials in 384 of the 1,102 programs listed in the 1979 Catalog of Federal Domestic Assistance. These programs contained both procurement and assistance transactions. Our sample included programs administered by 48 of the 57 Federal agencies listed in the Catalog. The questionnaire was applied during May and June, 1980.

From the questionnaires we compiled data showing the number of programs where

--responsible officials knew of the act,

--plans have been made or carried out to implement the act, and

--changes have occurred in the type of instruments used in the program.

The questionnaire also produced data on the criteria Federal officials use to select the type of instrument used in these programs and indicators of the effectiveness of the act in achieving its purposes. Because we used a stratified sample in obtaining the

---

1/In the 97th Congress the name of the Subcommittee was changed to Subcommittee on Federal Expenditures, Research and Rules.

data, we applied weights to project the data to the universe of assistance programs. The various figures used in this report are our estimates based on these projections. We believe the projections present a reasonable picture of Government-wide implementation of the act. There is, however, an unknown margin of error because the Catalog neither contains all assistance programs, nor is it intended to contain procurement programs, such as Department of Defense weapon system procurement.

To develop general information on Federal agencies' activities and problems, we interviewed top department officials in 10 agencies who were appointed as agency liaisons with OMB for matters relating to the act, and we reviewed appropriate files. We also interviewed top agency procurement officials in agencies where these officials were not the liaisons with OMB.

To obtain specific information on how the act was being applied and on issues arising from such application, we interviewed responsible officials in 21 programs. For 10 of the 21 programs, we examined how they were managed at the regional level. We generally reviewed up to 10 transactions per program and then selected 1 specific transaction in each of the 10 programs for more thorough review, including field work with the recipient. We performed this work at Federal regional offices in Kansas City, Kansas; and Philadelphia, Pennsylvania. The programs reviewed were selected to develop particular issues identified during preliminary work conducted in 16 Federal agencies during calendar year 1979. Since these programs were not selected to represent the universe of Federal programs, the findings specific to them cannot be projected to all programs.

## CHAPTER 2

## INCORRECT INSTRUMENTS CAN BE CHOSEN BECAUSE GUIDANCE IS VAGUE

Two major problems the Congress sought to correct through the act are not being adequately addressed. First, because assistance instruments are being used in procurement situations, Federal procurement requirements designed to protect the Federal interest and maximize competition may not be applied. Second, because Federal officials are not systematically examining assistance relationships in selecting either grants or cooperative agreements, there is no certainty that officials are limiting requirements in assistance awards to those consistent with the intended relationship.

Several revisions to OMB's guidance are necessary to improve the act's implementation and to achieve consistent Government-wide selection of appropriate legal instruments. Currently, OMB's guidance on several of the act's key provisions, although a good first step, is too vague and incomplete. Consequently, Federal officials interpret these provisions in varying ways, some of which we believe are incorrect.

OMB currently has several task forces studying potential revisions to its guidance and is in preliminary agreement with us on several issues discussed below.

### CLEARER TERMS AND PROCEDURES NEEDED TO DISTINGUISH BETWEEN PROCUREMENT AND ASSISTANCE

One of the basic purposes of the act was to curb the use of assistance instruments in procurement situations. The inappropriate use of assistance instruments in procurement situations was considered a problem for more than one reason, but primarily because certain procurement requirements, such as competition, were often avoided by using assistance instruments. Thus, qualified bidders may be excluded from consideration or low-quality products may be delivered without Government recourse.

During our review of individual agency awards made since passage of the act, we found several actual or proposed assistance awards which we believe should have been procurement contracts. Most of the proposed or actual awards were cooperative agreements. In other recent audits, we also found assistance awards that we believe should have been procurement contracts. Because of the general misunderstanding of key provisions of the act, we believe the potential exists for many questionable awards.

The act's terms and legislative history and OMB's implementing guidance have fostered inconsistent interpretations. In analyzing the act and its history, and after frequent discussions with OMB and congressional staff, we have developed an interpretation that we believe yields results consistent with congressional purposes. This interpretation is the basis for our disagreement with some Federal officials' use of assistance instruments rather than procurement contracts.

The act distinguishes between procurement and assistance relationships based on the authorized Federal purpose. If the Federal purpose is to acquire something, a procurement relationship is appropriate. If the Federal purpose is to accomplish a public purpose of support or stimulation as authorized by statute, either a grant or cooperative agreement relationship is appropriate depending on the anticipated degree of involvement with the recipient.

Determining the scope of an agency's authority to either procure or assist is essentially a matter of statutory interpretation to answer the question, "Can the organization spend money as it proposes?" Common sources of this authority include the agency's organic legislation, enabling statutes, or appropriation acts. The Federal Grant and Cooperative Agreement Act's legislative history also refers to agency "mission" statements as a source for determining whether an agency is authorized to engage in assistance activities. In sum, defining an agency's authority in a given case may require reference to a range of materials. By enacting specific authorizing language and providing various sources to help an agency understand this language, the Congress is also implicitly describing the limitations on authority--the Congress has authorized this much and no more. Therefore, an agency official's responsibility when considering a proposed assistance award includes deciding whether the agency has authority to enter into the particular assistance transaction. This decision must be made for each transaction because procurement authority is available in all assistance programs and any given transaction might be either procurement or assistance.

Applying these distinctions in practice has been anything but simple, in part because the act is not a model of clarity. Thus it is not too surprising that Federal agencies interpret and apply the criteria in various ways and continue to use grants and cooperative agreements in what appear to be procurement situations.

However, the Congress recognized that the criteria were primarily a first step in clarifying difficult concepts. Accordingly, it authorized OMB to issue supplementary interpretative guidelines. We believe the vagueness in the act can be overcome by improved OMB

guidance and a more structured analysis by Federal agencies to determine what instrument best reflects the relationships to be established.

One of the cooperative agreements we reviewed, for example, contained provisions which clearly indicated to us that the agency was purchasing products or services and should have used a contract. Among other things, the recipient was to:

--Inventory recipients' training materials, get them well-edited, and ready for the agency's approval, production and distribution. [service culminating in a product]

--Hold the agency's annual evaluation conference and manage one other conference. [service]

--Assist the agency to develop two Request For Proposals and assist in selecting contractors. [service]

--Assist the agency in completing a manual it had drafted and complete a plan for distributing and using the manual. [service and product]

We believe the relationship described in the foregoing example is clearly procurement in nature. But in this and other cases some agencies believe there is some basis for arriving at contrary decisions. The variations in how agencies choose between a type of procurement contract or assistance instrument stem from their interpretations of sections 4(1) and 7(a) of the act. Section 4(1) sets forth the criteria on when to use a type of procurement contract. Section 7(a), as we see it, overcomes the problem many agencies face when imprecise use of terms in authorizing legislation restricts them to using a particular instrument where the program statute clearly intended another relationship. Section 7(a) authorizes the use of the act's instruments which are appropriate to the actual relationships available under the program statute, and which satisfy the criteria of the act.

Problems interpreting section 4(1)

Section 4(1) states that a type of procurement contract shall be used "* * * whenever the principal purpose of the instrument is the acquisition, by purchase, lease, or barter of property or services for the direct benefit or use of the Federal Government."

Some officials key on the "direct benefit" language of this section and interpret it to mean that the Federal Government must benefit more than anyone else if procurement is to be used. If they conclude that someone other than the Federal Government is going to benefit more than the Government, they believe a grant

or cooperative agreement is appropriate. When determining who benefits, officials sometimes take into consideration not only whether the immediate recipient of the award benefits, but also whether other parties may benefit. For example, in commenting on a cooperative agreement issued to a university for evaluating a Federal agency program, a Department of Housing and Urban Development (HUD) official noted that the cumulative benefit to the (1) university researchers, (2) program recipients, and (3) general public outweighed the benefit to the Federal Government.

In our opinion, this interpretation of direct benefit is questionable. In practice, this approach adds another criteria--benefit to the recipient or other parties--for when a grant or cooperative agreement can be used. In passing the act, the Congress sought to restrict agencies to the use of the act's criteria when selecting a grant or cooperative agreement. To this end, the Congress specified that a grant or cooperative agreement is to be used if the agency's principal purpose in a given transaction is to transfer something of value to a recipient to accomplish a public purpose of support or stimulation authorized by Federal statute.

This direct benefit interpretation, in combination with other factors, has also been applied in transactions involving so-called intermediaries. An intermediary situation often arises where an assistance relationship is authorized with certain parties, but the Federal agency delivers the assistance by utilizing another party. This "intermediary" thus is the recipient of the Federal award. For example, the Community Services Administration (CSA), which frequently provides assistance to community action agencies that lack computer expertise, has considered entering into a relationship with a firm (an intermediary) to prepare guidance manuals for distribution to community action agencies. CSA officials contend that a procurement contract is not appropriate in these circumstances because the Federal Government does not benefit directly, as it does not directly receive the product or service or it receives only an informational copy. CSA as well as other officials following this approach seem to feel that the Government must take direct possession of the product or service before a procurement contract is required.

This approach, in our view, reflects a misunderstanding of section 4(1). Our interpretation of the act is that the choice of instrument for an intermediary relationship depends solely on the Federal purpose in the relationship with the intermediary since it is the recipient of the Federal award. The fact that the product or service produced by the intermediary pursuant to the Federal award may flow to and thus benefit another party is irrelevant. What is important is whether the Federal Government's purpose as defined by program legislation is to acquire the intermediary's services, which happen to take the form of producing the product or carrying out the service that is then delivered to the assistance recipient, or if the Government's purpose is to

assist the intermediary to do the same thing. In other words, where the recipient of an award is not an organization that the Federal agency is authorized to assist, but is merely being used to provide a service to another entity which is eligible for assistance, the proper instrument is a procurement contract.

We recognize that such distinctions are not always clear. However, an analysis by each agency of its program legislation is an essential first step in determining which instrument it may choose. Such an analysis may not resolve all difficulties, but it will often ease the task of choosing between procurement and assistance. Program legislation often specifies

--whether an agency is to conduct a basic program activity itself or is to help (i.e., support or stimulate) someone else to perform the activity;

--who are the eligible recipients; and

--what the funds can be used for.

As discussed on page 8, only when an agency has statutory authority to support or stimulate someone else can it use a grant or cooperative agreement, 1/ and then, only for the recipients and purposes authorized. This constitutes the scope of the agency's assistance responsibilities. Basically, except where this kind of authority is present, the agency is responsible for performing all other actions itself or through procurement contracts and other arrangements authorized by law.

Applying the criteria outlined above to actual or proposed agency awards raises questions as to the appropriateness of their instrument choices.

For example, the Rural Electrification Administration (REA), announced in the June 1979 Federal Register that it was making funds available "for the partial financing of a research and development project to develop and make available on the market a direct burial splice closure for buried telephone cable * * *." On September 21, 1979, REA awarded a grant for the cited purposes to a private company which manufactures telecommunications cable.

REA is a Federal lending agency that finances electric and telephone facilities in rural areas. The REA Administrator's authorities in relation to telephone service are specified in Title II of the Rural Electrification Act:

---

1/An agency may, of course, be authorized to assist someone through use of other means, such as loans, direct payments, or subsidies.

> "* * * the Administrator is authorized and empowered to make loans to persons now providing or who may hereafter provide telephone service in rural areas, to public bodies now providing telephone service in rural areas, and to cooperative, non-profit, limited dividend, or mutual associations."

The REA grant award does not appear to fall within the scope of this authority since (1) the authority is specifically for the provision of loans, and (2) those eligible for loans must either provide or plan to provide telephone service in rural areas. The recipient of this REA award does not provide such services, but rather supplies materials to those that do.

REA indicated in its Federal Register announcement that under Section 11 of the Rural Electrification Act and under the Federal Grant and Cooperative Agreement Act, the Administrator can make such expenditures as are appropriate and necessary to carry out the provisions of the Rural Electrification Act. Section 11 provides in part that

> "The Administrator is authorized * * * to make such expenditures (including expenditures for personal services; supplies and equipment; lawbooks and books of reference; directories and periodicals; travel expense; rental at the seat of government and elsewhere; the purchase, operation, or maintenance of passenger-carrying vehicles; and printing and binding) as are appropriate and necessary to carry out the provisions of this act."

Although section 11 authorizes REA to make expenditures to conduct its operations, we do not believe that this constitutes an authorization to support or stimulate as contemplated by the Congress in the Federal Grant and Cooperative Agreement Act. Nor do we believe, as discussed later, that the act itself authorizes agencies to undertake activities not previously authorized by enabling statutes.

In another example, the National Institute of Corrections (NIC), administratively placed under the Bureau of Prisons, Department of Justice, planned to use a cooperative agreement to hire an accounting firm to pay its bills. Our analysis of the program's legislation, within the context of the Federal Grant and Cooperative Agreement Act, indicates that a type of procurement contract rather than a cooperative agreement was appropriate. NIC's legislative history notes that it is to be a national center to which State and local correctional agencies can look for the many different kinds of assistance they require. It partially fulfills its responsibility by engaging consultants to assist correctional agencies.

In the July 1980 Federal Register, NIC announced its intention to make an assistance award "to provide management accounting and recordkeeping functions for NIC Training and Consulting Projects." As explained by NIC officials, a cooperative agreement would be awarded, probably to a certified public accounting firm, and the recipient would make payments to NIC's consultants upon authorization from NIC. As succinctly stated by a former Department of Justice internal auditor, the recipient of the cooperative agreement would "pay NIC's bills."

NIC staff offered several reasons for the choice of a cooperative agreement, including:

--NIC would be substantially involved with the recipient, and such involvement would not be appropriate under a contract.

--The department's internal audit staff had questioned the choice of a grant but had indicated either a contract or a cooperative agreement would be appropriate.

--A contract would not be appropriate because NIC is not the recipient of the services (i.e., expense checks for the consultants) and therefore NIC does not directly benefit.

The third reason offered, that NIC is not to be the recipient of the services produced under the cooperative agreement illustrates, as previously discussed, how some officials believe that they must take direct possession of a product or service for a procurement contract to be the required instrument.

The Department of Justice's Internal Audit staff did, as indicated in the second NIC reason, question NIC's use of a grant to fund a certified public accounting firm for these purposes. The audit report noted that "a grant solely for the purpose of processing payments to consultants seems to provide a direct benefit to the government since processing payments for services received is a normal function of a Federal agency." However, contrary to NIC's assertion, the audit report did not actually suggest that a cooperative agreement would be appropriate. Rather, by noting that section 4(2) provides for the use of a contract "whenever an executive agency determines in a specific instance that the use of a type of procurement contract is appropriate," the report appears to suggest that a contract should have been used for these services.

The Department of Justice auditor who performed the survey of NIC's activities said that although he believed NIC was clearly purchasing the services of the public accounting firm, after reading the act he did not feel he could make a sufficiently strong

case to say a contract had to be used. His doubt was based on an understanding that NIC was in fact substantially involved with the recipient and thus he believed a cooperative agreement might be appropriate. In fact, when choosing between procurement and assistance, the degree of anticipated involvement does not matter; the choice is governed solely by the Federal purpose in the relationship.

Department of Justice officials we interviewed about this award were familiar with NIC's legislation and said that NIC has broad authority to use either grants or contracts. In response to our questions, one NIC official noted that the following section of its legislation conferred broad authority:

> "In addition to the other powers, express and implied, the National Institute of Corrections shall have authority--
>
> (1) to receive from or make grants to and enter into contracts with Federal, State, and general units of local government, public and private agencies, educational institutions, organizations, and individuals to carry out the purposes of this chapter." (18 U.S.C. 4352(a)(1).)

Although this section does provide broad authority, we do not believe it is applicable to the situation contemplated in the proposed cooperative agreement. Senate Judiciary Committee Report 93-1101 on NIC's authorizing legislation explains that section 4352(a)(1) "would enable the Institute to benefit from the resources and expertise of such agencies * * * who have been active in supporting correctional reform efforts." Public accounting firms, expected to perform accounting services, do not meet this test.

However, the Congress did include a specific authorization in NIC's legislation that we believe is directly applicable to the proposed cooperative agreement. It provides that NIC shall have authority:

> "to enter into contracts with public or private agencies, organizations, or individuals, for the performance of any of the functions of the Institute * * *." (18 U.S.C. 4352(a)(13).) (Emphasis added.)

That the tasks to be performed under the proposed cooperative agreement are functions of the Institute seems clear. This was the conclusion of the internal audit staff as noted above. The audit report also notes that NIC formerly performed these functions itself. The Federal Register announcement also leads to this conclusion in stating that the project is "to provide management accounting and recordkeeping functions for NIC * * *."

Finally, the NIC official listed in the Register as an information contact said that everyone agreed the activities covered under the announcement were an in-house function, but because their requests to OMB for additional staff had been turned down they could not perform the functions themselves.

Problems with section 7(a)

Our review of agencies' decisions on when to use a type of procurement contract, grant, or cooperative agreement indicated the potential exists for misinterpretations of section 7(a). The problem centers on whether this section gives agencies broad new independent authority to choose to offer assistance where there was no authority to enter into such an assistance relationship previously.

Although we identified only two cases where we believe a misunderstanding of section 7(a) directly contributed to a questionable change in instruments, the potential for many other questionable awards exists on the basis of the general misunderstanding of this section.

Section 7(a) of the act states:

> "Notwithstanding any other provision of law, each executive agency authorized by law to enter into contracts, grant or cooperative agreements, or similar arrangements is authorized and directed to enter into and use types of contracts, grant agreements, or cooperative agreements as required by this Act."

If the legislative history concerning section 7(a) is read within the context of the general congressional purposes for the act, it does not appear that the Congress intended any wholesale expansion of grant authority. Rather, it appears that the Congress only intended to require agencies to use an instrument that matches the relationship they enter into, regardless of the label used in existing legislation to characterize that relationship. In our opinion, the act was not intended to change the nature of the relationships authorized in existing legislation.

OMB's guidance on section 7(a) can be construed as supporting the interpretation that section 7(a) supersedes program authorizing legislation and in itself provides authority to use any of the three instruments.

One portion of the act's legislative history which is closely paraphrased in OMB's guidance, states:

> "If an agency is presently authorized only to enter into either contracts, grants, cooperative agreements or other arrangements, this authorization enables that agency to enter into any or all three types of agreements subject to the criteria set forth in sections 4, 5, and 6. However, if an agency is specifically proscribed by a provision of law from using a type of agreement, this authorization would not affect that prohibition."

Another passage says that agencies will have flexibility in determining whether transactions are procurement or assistance.

We believe that section 7(a) gives agencies a very circumscribed authority to overcome prior instrument restrictions that were not consistent with the relationships described by program legislation. The act's legislative history, dating back to the Commission on Government Procurement, reflects a concern that program statutes often restrict agencies to a type of instrument that is inconsistent with the overall relationship described in the statute. Through the act, the Congress sought to correct this situation. First, sections 4, 5, and 6 provide Government-wide criteria to be used in selecting instruments. In our opinion, the Congress fashioned section 7(a) to deal with those cases where, lacking such criteria, the Congress had unintentionally restricted an agency to using a specific instrument which did not fit the type of relationship described in the statute itself. The following passage from Senate Report Number 95-449, partially explains section 7(a).

> "The proposed legislation does not automatically change the type of instrument authorized by statute but rather authorizes the agencies to use other instruments if appropriate and consistent with this bill. The legislation is not intended to nor will it eliminate specific program or administrative requirements placed by the Congress in individual program statutes. It also will not eliminate specific requirements applying, for example, to grants in such organic statutes as the Work Hours Standards Act. Given the foregoing understanding, it is not practical or necessary to identify all of the statutes which might be somewhat affected."

In short, the Congress did not consider it necessary or practical to tackle the enormous housekeeping problem of going through each piece of authorizing legislation and inserting, where the guidelines of the Federal Grant and Cooperative Act made it appropriate, the words grant, cooperative agreement, or contract. Rather, the Congress left it to the executive branch agencies to analyze their particular authorizing statutes. Under this approach, to find "grant" or "cooperative agreement" authority in each agency's authorizing statute, where these specific words of authority have

not been used, it must be determined what kind of relationships the agency's statute authorizes: namely, in order to find grant authority, the authorizing legislation must be examined to determine if a grant type relationship was intended or permitted rather than simply looking for the word "grant." If the Congress had intended that section 7(a) authorize agencies to use grants, cooperative agreements, or contracts irrespective of the basic relationships authorized by prior program legislation there would have been no need to state that the act "does not automatically change the type of instrument authorized by statute." Thus, we believe section 7(a) is intended to function as is illustrated hypothetically in the following table.

| Prior enabling legislation | Change due to section 7(a) |
|---|---|
| 1)Hypothetical authorization:<br><br>"Agency X shall determine which local governments suffer most due to the inequitable impact of energy development and provide such financial and technical assistance as is necessary to mitigate such impact. In providing such assistance, the administrator is authorized to enter into contracts with such local governments or public or private organizations as he deems necessary." | Since the last sentence in this hypothetical authorization limits the administrator to the use of contracts even though the relationship with the local governments is clearly assistance, we believe section 7(a) allows the second sentence to be interpreted as follows:<br><br>"In providing such assistance, the administrator is authorized to enter into grants or cooperative agreements with such local governments or other public or private organizations as he deems necessary." |
| 2)Hypothetical authorization:<br><br>"Agency Y shall identify those individual veterans who, for whatever reason, have not been adequately provided job training and shall provide them with the necessary training to make them competitive in the job market. In providing such training, the administrator may utilize agency employees, may hire new employees, or may contract with public or private organizations." | Since the agency responsibility delineated in this authorization is to provide the training itself, section 7(a) does not authorize the agency to use grants or cooperative agreements with public or private organizations. |

Our interpretation of section 7(a) was well expressed in a legal memorandum by the Department of Energy's Acting General Counsel:

> "Indeed, it seems clear that the FGCAA was not intended to permit an agency, in implementing any program, to transcend the discretion which was conferred upon it by the enabling law, but only to carry out the purposes of that law more efficiently. That is, the FGCAA is not a "bootstrap," and may be relied upon to enhance agency prerogatives only after the objectives of the enabling law have been appropriately characterized, not before. 4/ In some instances, it will be difficult to make this characterization, and legislative history and judicial decision may need to be invoked. But in each case, it will be the four corners of the enabling law, and not the FGCAA, which will establish the parameters of the relationship between Federal and non-Federal parties. The FGCAA may then be utilized so that the law can be implemented without regard to ill-defined nomenclature in the enabling law which may, for that reason alone, hamper an agency's ability to give effect to Congress' intent." (Footnote omitted.)

Officials who do not share this view have used section 7(a) to justify the use of assistance instruments for transactions which otherwise would appear to call for use of procurement contracts. For example, prior to the act, the Environmental Protection Agency (EPA) used contracts in its Epidemiologic Studies program. Although this necessitated following certain procedures which EPA officials believed were time consuming and objectionable to both EPA and recipients, EPA officials considered themselves to be statutorily restricted to procurement contracts. After the act became effective, EPA began using cooperative agreements instead of contracts. EPA officials told us that this change was due, among other reasons, to their belief that section 7(a) gave them authority to use grants, contracts, or cooperative agreements. Our interpretation of EPA's authority under this program indicated there is some justification for use of assistance instruments. However, EPA officials said they had not specifically reviewed their legislation for the presence of such authority but relied on their interpretation of section 7(a) and other factors. Interestingly, although there appears to be some justification for using assistance instruments, both EPA program officials and a recipient of a cooperative agreement told us they viewed the research being conducted as primarily for EPA's benefit or use in connection with its responsibilities for monitoring and regulating pesticides, suggesting that a contract would continue to be the appropriate instrument.

Although an analysis of program authorizations to determine what type of relationship the Congress intended should resolve

many of the current problems in selecting instruments, there are authorizations which permit agencies to exercise broad discretion in designing relationships to achieve particular objectives. Therefore, if in reviewing its enabling legislation an agency determines its authorization is broad, it then becomes necessary to determine which of the instruments authorized by the act most closely match the agency's purpose in a proposed transaction. For example, the Secretary of HUD has broad authority to:

> "undertake such programs of research, studies, testing, and demonstration relating to the mission and programs of the department as he determines to be necessary and appropriate."

Because the Secretary is neither directly mandated to do this work with HUD staff, nor mandated to assist others to do such work, but rather is given authority to undertake "programs," the Secretary has considerable discretion. This discretion is reinforced through a provision stating the Secretary may perform such duties "either directly or * * * by contract or by grant."

Pursuant to this authorization, HUD officials determined that there was a need to document and disseminate information about urban insurance availability "in order to stimulate local government involvement in these issues." Lacking in-house resources and technical expertise, HUD identified a firm that could do the work. A noncompetitive cooperative agreement was awarded to the firm to

--produce a guidebook on local insurance problems for HUD distribution to local governments;

--conduct two regional workshops to familiarize local government officials with strategies to analyze and resolve insurance problems; and

--conduct a briefing for key Federal officials, interest groups, and industry representatives.

In summary, HUD officials recognized an agency responsibility to assist the local governments, but lacking an in-house capability to do so, acquired the services of a firm to help the agency discharge its responsibility. Although the statutory authorization under which the work was performed is broad, we believe the relationship itself is one of procurement and, on the basis of the act's criteria, a procurement contract should have been used.

Finally where program authority can justify a choice of instruments and it is difficult to say that assistance or procurement is the principal purpose of the transaction, agencies have discretion and should exercise the discipline noted in the legislative history of the act in their choice of instruments. It should be

kept in mind, however, that the first-level analysis of agency authority to enter into the kind of transaction envisioned is not really a matter of discretion--the statutory authority is either there or is not there, regardless of agency preference. We recognize that agency authority may be difficult to determine and require the exercise of a substantial amount of judgment.

## Agencies usually supplement, or do not use, the act's criteria when selecting instruments

The Federal Grant and Cooperative Act contains the only criteria Federal officials are supposed to use when selecting instruments. But many officials do not use the criteria or supplement it with their own criteria when deciding what instrument to use.

On the basis of our telephone survey we estimate that 77 percent of Federal officials use a mixture of the act's criteria and other criteria when choosing between procurement and assistance instruments. Another 8 percent do not rely at all on the act's criteria when making their choices. Our detailed review of selected programs produced similar evidence that officials use criteria in addition to that in the act.

The use of these additional criteria seems to influence agencies toward the selection of assistance instruments. As previously discussed (see p. 10), Federal officials, in effect, use criteria not in the act when they make assistance awards because someone else benefits more than the Government from a relationship. Officials also told us that in deciding which instruments to use they consider factors such as potential adverse program effects, preferences of recipients, and the degree of administrative flexibility available under the type of instruments. For instance, one program director told us that, although certain aspects of the program indicate a cooperative agreement would be appropriate, a change from grants to cooperative agreements would upset recipients and endanger the program's success. An assistance policy official in another agency also noted that while the official departmental policy is to adhere to the act's criteria, the preferences of recipients "count."

Some other officials indicated that the need for more effective control over recipients' actions is considered in selecting instruments. In such cases, they generally believe contracts are appropriate.

Federal officials' reliance on other criteria when selecting contracts, grants, or cooperative agreements runs directly counter to the act's purpose of achieving uniformity in the use of such instruments. Although OMB's guidance contains an explicit statement limiting agencies to using the act's criteria when choosing

between grants and cooperative agreements, it does not contain a similar direct limitation for choosing between procurement and assistance.

## NEED TO IMPROVE COOPERATIVE AGREEMENT GUIDANCE

Two years after OMB issued its guidelines, officials of Federal agencies, OMB, and we, ourselves, do not clearly understand what a cooperative agreement is, when to use it, and what to use it for. Thus, Federal officials are not always systematically identifying the type or degree of their involvement with a recipient. Identification of this involvement could lead to a reduction in unnecessary administrative requirements in assistance awards.

The act provides that the factor to consider in deciding whether a cooperative agreement is appropriate, as opposed to a grant, is whether the Federal agency will be substantially involved during recipient performance. Although a good first step, OMB's guidelines do not adequately define and distinguish substantial involvement, normal involvement, and normal Federal stewardship. As a result, Federal agencies find it difficult to apply the criteria when deciding what instruments to use in their programs.

We recognize the difficulty in developing Government-wide guidelines that will yield uniformity in the use of grants, contracts, and cooperative agreements. As discussed in chapter 4, differences in operating procedures must be developed for these instruments in order to make the distinctions meaningful. This may take considerable time and effort. In the meantime, interim revisions to OMB's guidance would seem desirable to gain the operating experience needed to develop the necessary distinctions, and standardize grant/cooperative agreement decisions within programs and agencies.

### Difficulty in developing Government-wide guidelines for cooperative agreements

OMB had two basic problems when it prepared the guidelines on cooperative agreements and which face it now as it works to revise them. First, because the Congress wanted the instrument to evolve with agencies' experience, it did not thoroughly describe what a cooperative agreement is, nor when and how it should be used. Second, adequate data was not available on practices and procedures used by Federal agencies to manage assistance awards. Combined, these problems made it very difficult to develop guidelines which would clearly distinguish between grant and cooperative agreement relationships.

The Congress' intent in establishing the cooperative agreement as a category of existing assistance relationships originated in the findings of the Commission on Government Procurement. The Commission concluded that a cooperative agreement category was essential for reducing the confusion in deciding when to use grants or contracts. The Commission found that the need to be more involved with assistance recipients than was customary in grant relationships was leading agencies to use contracts in assistance relationships. The cooperative agreement category was viewed as a recognition that the Federal Government was sometimes closely involved with assistance recipients. In addition, the Commission saw other advantages in dividing assistance relationships into two categories:

--Clarification of Federal and recipient roles and responsibilities based on different expected levels of involvement.

--Increased consistency in Federal interactions with recipients.

--An initial basis for making the Federal assistance system more rational, possibly along lines analogous to the procurement system.

As a criteria for distinguishing between grants and cooperative agreements, the Commission proposed using the amount of Federal involvement with the recipient during performance of the supported activity. Little involvement would equate to a grant, and substantial involvement would equate to a cooperative agreement.

The Commission was not explicit, however, on what constituted substantial involvement. On the basis of explanatory text in the Commission's report and examples of cooperative agreements, the Commission seemed to see substantial involvement in two senses: (1) when Federal and recipient officials work closely together, and (2) when Federal officials need to closely oversee a recipients' activities to ensure that the program's objectives are achieved.

The Congress accepted the Commission's recommendation and included the cooperative agreement category in the act. However, the legislative history provides little elaboration on the Commission's explanation of cooperative agreements or how to determine when to use them. Committee reports cite the same examples used by the Commission to illustrate when a cooperative agreement would be used. Recognizing that more definitive guidance was needed for agencies to follow in selecting cooperative agreements, the Congress charged OMB with interpreting the act's criteria for choosing between grants and cooperative agreements. Until better guidance was developed, the Congress only expected that agencies would be able to reasonably justify their instrument choices.

In addition to the congressional intent that the instruments would evolve with agencies' experiences, adequate data on agency practices and procedures was not available to assist OMB in developing an initial set of Government-wide standards for uniform selection of cooperative agreements. Prior surveys of Federal agencies' operating practices were not comprehensive enough or were not directed to the development of standards to identify or measure substantial involvement during performance. Further, the work of the Procurement Commission and others, although extensive, did not comprehensively survey agency practices in administering their assistance programs. Thus, in developing guidelines, OMB relied for the most part on experiences of Federal officials obtained through discussions and circulation of draft guidance. This approach worked reasonably well as a first step, but further efforts are needed to refine the guidelines to make them more useable.

## Problems facing Federal officials in identifying cooperative agreements

A number of Federal officials have used OMB's guidelines as a basis for issuing cooperative agreements in their programs. However, most Federal officials we talked to have difficulty applying the guidelines because their decisions must be based on relative standards like "substantial involvement" and "normal Federal stewardship" which are not adequately defined. As a result, these officials have a difficult time identifying situations where a cooperative agreement should be used.

OMB's guidelines state that anticipated substantial involvement during performance is a relative rather than an absolute concept. The guidelines establish a general policy that substantial involvement is not anticipated when the terms of an assistance award indicate the recipient can expect to run the project without Federal agency collaboration, participation, or intervention as long as it is run in accordance with the terms of the instrument. Conversely, substantial involvement is anticipated when the terms of the instrument indicate the recipient can expect Federal agency collaboration or participation in the management of the project.

As a guide to making these determinations, OMB provided eight illustrations of agency practices and procedures where substantial involvement could be present depending on the circumstances of a particular award. Federal officials are to relate specific program procedures to these indicators of substantial involvement in determining whether their practices exceed the normal exercise of Federal stewardship responsibilities.

The guidelines, however, do not define involvement or clearly establish how normal Federal stewardship differs from, or is similar to, substantial involvement. The guidelines also do not indicate which individual indicator or combination of indicators,

requires the use of a cooperative agreement. Thus, a decision to use a cooperative agreement is a very subjective exercise.

Instead of clarifying substantial involvement, the guidelines may tend to confuse Federal officials and thus limit the use of cooperative agreements. The guidelines state that anticipated substantial involvement does not include the exercise of normal Federal stewardship responsibilities during the project period, such as site visits, performance reporting, financial reporting, and audit to insure that the objectives, terms, and conditions of the award are accomplished. This causes Federal officials to consider their management and oversight practices, even though more extensive in some cases than others, as "normal" and to conclude that they are therefore not substantially involved. They view the typical grant relationship as one of carrying out their responsibility to make sure recipients spend Federal funds for the purposes intended and comply with other conditions of the award. As a result, their involvement with a recipient takes on an air of legitimacy, making it difficult for them to see that they may be substantially involved with some recipients. Consequently, they are less likely to evaluate the appropriateness and need for that level of involvement.

For example, the Community Services Administration (CSA) has extensive rules and procedures for funding and evaluating its recipients. However, CSA officials said these rules and procedures and related monitoring could not be considered substantial involvement because CSA is carrying out its statutory obligation to oversee how Federal funds are spent. They also said the OMB guidelines excluded efforts to see that rules and procedures are carried out because these efforts are an exercise of normal Federal stewardship responsibilties.

This interpretation can lead agencies to overlook indicators of substantial involvement. The Department of Transportation's Urban Mass Transportation Administration (UMTA), for example, considers its extensive control and evaluation of recipients a part of normal Federal stewardship. But UMTA procedures appear to relate to at least one of OMB's indicators of substantial involvement suggesting that cooperative agreements may be appropriate. The OMB indicator pertains to Federal involvement in the awarding of subgrants or subcontracts by a recipient of Federal assistance. It suggests that reviews and approvals which exceed existing OMB policies on Federal oversight of grantee procurement standards and sole source procurement be considered as potential substantial involvement. UMTA officials acknowledged that their procedures of regular review of proposed subawards go beyond the cited OMB policies.

The difficulties Federal officials have in applying the OMB guidelines are illustrated by differences in opinions between Federal officials within the same agency. For example, the announcement for EPA's solid waste resources recovery program stated

that cooperative agreements should be used because close interaction and cooperation between EPA and recipients is required. Regional officials, however, said such EPA involvement occurred only during the planning phase and therefore grants might be more appropriate.

The difficulty in applying the guidelines to specific programs was readily apparent to us from our discussions with OMB. What appears to be normal Federal stewardship to one person could be substantial involvement to another depending on their individual frame of reference. The OMB indicators of substantial involvement were intentionally broad. OMB did not want them to be viewed as a checklist but rather as a frame of reference for agencies to assess the level of involvement in their programs. Although appearing to be a practical approach, agencies have had difficulty applying these broad indicators to specific operating practices in their many and varied programs.

For example, the OMB guidelines state that substantial involvement may be present when the relationship includes Federal:

> "review and approval of one stage before work can begin on a subsequent stage during the period covered by the assistance instrument."

An official of the Health Standards Quality Review Bureau of the Department of Health and Human Services (HHS) described to us how his agency reviews and approves recipient plans for implementing medical reviews. These plans evolve through interaction between HHS and its recipients, but the official was not certain if this constitutes approval of stages as described in the OMB guidelines.

We discussed this and several other examples with OMB officials and had difficulty determining how the substantial involvement indicator applied. After considerable discussion, an OMB official responsible for the guidance concluded that stages of work are present when, in a project

--segments are integrated and have one clearly defined overall output,

--each segment clearly follows the preceding segment and is directly linked to it, and

--the segments fall within one funding period.

With this amplification of the criteria it was easier to apply the indicator to specific examples. However, further work still needs to be done. Although subjective judgments will always be present in arriving at these decisions, we believe OMB can reduce the amount of subjectivity by better defining the various kinds of involvement and expanding on the indicators of substantial involvement.

We also believe one of the indicators of substantial involvement is overly qualified and excludes significant Federal involvement from consideration when the selection is made between grants and cooperative agreements. According to the guidelines, involvement could be substantial where the relationship includes:

> "Highly prescriptive agency requirements prior to award limiting recipient discretion with respect to scope of services offered, organizational structure, staffing, mode of operation, and other management processes, coupled with close agency monitoring or operational involvement during performance over and above the normal exercise of Federal stewardship responsibilities to ensure compliance with these requirements."

Initially, the indicator presents the same problem discussed above concerning what is normal Federal stewardship. In addition, the indicator applies only when the highly prescriptive requirements are coupled with close agency monitoring or operational involvement during performance.

In our opinion, highly prescriptive requirements themselves can, if they significantly restrict how a recipient must do something, indicate that the Federal agency is substantially involved during performance. Simply because these requirements are placed on the recipient prior to award does not alter the fact that the recipient has limited discretion, during performance, to manage the program or project involved. Further, the manner in which the requirements are monitored is not pertinent; they effectively limit what the recipient can do and increase the Federal presence. We believe that, among other things, the Congress had this type of Federal/recipient relationship in mind when it created the cooperative agreement category.

Suggested approach to further defining substantial involvement

Until specific operational characteristics are developed distinguishing grants and cooperative agreements, it will be difficult to achieve Government-wide uniformity in the decisions on when and how they should be used. This is discussed further in chapter 4. In the interim, we believe it would be useful to develop an agency or program approach to defining normal or substantial involvement. This approach would promote standardized decision making at least at the program level, and possibly at the agency level. As this would still require use of the OMB indicators of substantial involvement as a frame of reference, it is not too unlike the way OMB and agency judgments are now made.

The key distinction would be that decisions on whether to use a grant or cooperative agreement would also hinge on whether recipients within a program, or among programs within an agency, are

treated differently. The feasibility of this approach is based on the fact that recipients of awards within many Federal assistance programs are treated differently depending upon such things as

--the capacity of a recipient to implement Federal programs without detailed Federal oversight, monitoring, and direction;

--prior Federal experience with a recipient; and

--the need for close Federal/recipient interaction to mutually contribute to achieving specific program objectives.

The first test in determining whether a cooperative agreement is appropriate for a given relationship would be whether or not the OMB indicators of substantial involvement are relevant. If that test fails due to problems previously discussed, the fact that a recipient is treated differently, that is, subjected to more controls and collaboration and has less discretion than the normal recipient for a given program, would suggest that the Federal agency is substantially involved and a cooperative agreement may be appropriate.

Where they do not now exist, standards could be developed by agency personnel for each program to promote uniformity in procedures and requirements. For example, HUD varies its involvement in the Community Development Block Grant (CDBG) program on a selective basis but does not generally consider its awards to be cooperative agreements. HUD CDBG program officials prepare a list of selected recipients representing the largest grantees and those grantees which have posed significant problems, such as poor performance and noncompliance with regulations. These recipients may be monitored extensively while other recipients may be monitored only once or twice annually. Also, program officials may require some of the identified recipients to complete activities in accordance with specified schedules or impose administrative or civil remedies, including requests for additional information and directions to discontinue activities and reprogram funds. Finally, if the lack of progress, compliance, or capacity is serious enough, a recipient may have a succeeding year's award reduced or given conditional approval.

HHS is another agency with a procedure similar to HUD's CDBG program approach. HHS has an agencywide "high-risk" procedure for problem recipients. A high-risk recipient is defined as one whose management practices raise serious questions about its ability to assure proper programmatic use and financial stewardship of grant funds. The criteria for identifying such recipients includes a history of unsatisfactory performance and material violations of

the terms and conditions of awards. Under the high-risk procedures, HHS requires monthly reporting and other special conditions which exceed normal policies and procedures. In addition to procedures to correct problems with a present recipient, Federal officials also become more involved when a new recipient has not demonstrated a capacity to perform. For example, ACTION officials provide more technical assistance and make more site visits when dealing with new recipients.

Of course, control purposes are not the only reason a Federal agency may be substantially involved with a recipient. Federal agencies often have cooperative relationships with recipients of their assistance awards that include frequent collaborative interactions to accomplish mutual objectives.

We believe that when Federal agencies vary their interactions as described above, they are often "substantially involved" in how a recipient administers an award. Because of the difficulties in applying OMB's guidance and their own perceptions of how much they are really involved, Federal officials often do not believe their involvement is substantial enough to require the use of cooperative agreements. One way OMB can address this problem on an interim basis is by instructing agencies to identify what is normal involvement for each of their programs and base their grant and cooperative agreement distinctions on whether they are more involved than normal with individual recipients in a given program.

The value of our suggested approach lies in its compatibility with, and foundation in, existing Federal administrative practices across many Federal programs. Thus, it is more likely to be accepted and implemented by Federal officials. This, in turn, will provide the data needed to start developing Government-wide standards. It also will provide an opportunity to compare the existing requirements for consistency with congressional intent and with the needs of a particular award.

We recognize, however, that some inconsistencies among programs will continue. Agencies that treat recipients differently but on the whole may be substantially involved with all recipients in a single program might characterize their normal recipient relationship as that of a grant. Likewise, agencies that treat recipients differently but may still not be substantially involved may use cooperative agreements with those recipients where their involvement is more than normal. To the extent agencies can relate the OMB indicators of substantial involvement to their programs, these problems should not occur. To the extent they cannot, they would at least have a more structured basis for their choices.

Inconsistent instrument choices could also be reduced by policy level reviews of the decisions program officials make under the interim approach. The policy level reviewer would judge

whether the normal level of involvement for a particular program is actually substantial compared to all other programs within the agency. If so, the program's normal awards would be cooperative agreements and if some awards have less involvement than the norm, they might qualify as grants. This approach would be in keeping with the requirement in OMB's guidance that program decisions be reviewed at a policy level.

OMB is working to revise its guidelines

In its March 1980 report to the Congress, OMB stated that its guidance could be made more precise and understandable based on agencies' experiences in implementing the act. OMB is now developing revisions and additions to its current guidance on grants and cooperative agreements to improve implementation of the act. The work is primarily being conducted by two task groups composed of Federal officials, private citizens, and representatives of interest groups under the overall direction of OMB. Several proposals have been developed by the task groups and are being considered by OMB.

The current OMB work addresses many of the matters discussed in this chapter and a number of other issues developed during the study of Federal assistance programs mandated by the act. We worked extensively with OMB to identify and develop these issues and to discuss potential revisions to the guidance. We also provided comments on the drafts developed by the task groups and the OMB staff. Our interaction with OMB has been very productive and, as a result, we believe a general consensus has developed between GAO and OMB regarding a basic interpretation of the act and how it should be applied to Federal procurement and assistance transactions.

CONCLUSIONS

The Congress established the act's criteria in part to promote Government-wide uniformity and increased discipline in the selection of procurement and assistance instruments. Although only two years have passed since the act has been in effect, it is evident that congressional purposes will not be fully realized unless OMB's guidance is improved. The current guidelines to distinguish between procurement and assistance do not clearly explain certain provisions of the act or outline a structured procedure for making decisions. As a result, Federal officials interpret key provisions of the act in ways we believe yield results inconsistent with congressional intent. Further, officials often inadequately review their authorizing legislation and frequently supplement or do not use the act's criteria when deciding which instruments to use.

Current guidance to distinguish between grants and cooperative agreements is also unclear and incomplete. The terms used by OMB to guide the decision between grants and cooperative agreements are

too vague for consistent application. Better definitions of normal involvement, normal Federal stewardship, and substantial involvement are needed to promote more consistent agency decisions.

Because data is lacking, and an understanding of the nature, purposes, and uses of cooperative agreements is still evolving, it may be some time before guidance to achieve Government-wide uniformity in the selection of cooperative agreements will be possible. As an interim measure, differentiations between normal and substantial involvement could be based on what is normal for each program and whether some recipients are treated differently from the norm. This approach will provide agencies with a more structured basis for defining this involvement and should produce more uniformity within each program, because it takes into account the fact that agencies vary their involvement depending on the recipient. Further improvements to OMB's guidelines could then be developed by studying the nature of involvement associated with the cooperative agreements.

OMB is taking steps to revise its guidelines. OMB staff generally concur with our interpretations of the act and what should be done to improve its implementation. The proposed revisions may be published in the next several months.

RECOMMENDATIONS TO THE DIRECTOR, OMB

To improve the selection of procurement contracts and assistance instruments, OMB should revise its guidance on the Federal Grant and Cooperative Agreement Act to:

--More clearly define the terms "direct benefit and use" as they relate to the selection of contracts and "accomplishing a public purpose of support or stimulation" as it relates to assistance.

--Require Federal program officials to base instrument choices on the Federal purpose in the relationship established after (1) reviewing their authorizing legislation to determine their authority to procure or assist, and (2) reviewing each proposed transaction in light of the act's criteria.

--Clearly state that section 7(a) of the act does not create new authority to make assistance awards independent of program legislation.

To help Federal officials identify potential awards where a cooperative agreement might be appropriate we also recommend that OMB revise its guidance specifically related to cooperative agreements. The revisions should:

--Define normal involvement, normal Federal stewardship, and substantial involvement. This could be accomplished by adopting our suggested interim program approach for assessing levels of involvement with program recipients.

--Recognize that highly prescriptive requirements prior to award limiting recipient discretion may constitute substantial involvement during performance whether or not they are coupled with close agency monitoring of, or operational involvement with, the recipient.

--Provide more detailed and complete illustrations of agency practices which can be considered as substantial involvement.

## AGENCY COMMENTS AND OUR EVALUATION

OMB and four of the responding Federal agencies generally agreed with our recommendations. With one exception, OMB is taking action to improve its guidance on how agencies should choose among procurement contracts, grants, and cooperative agreements. OMB disagrees, however, that highly prescriptive requirements may be an indicator of substantial involvement during performance whether or not they are coupled with close agency monitoring of, or operational involvement with, the recipient. This is discussed further below. The responses of other agencies ranged from general agreement with the thrust of the chapter to substantive disagreements on some points.

An analysis of the comments, particularly where major disagreements exist, and our evaluation follows. In cases where several agencies generally agreed with us or did not provide specific comments, we have concentrated on OMB's comments.

### Distinguishing between procurement and assistance

OMB agreed with our interpretation of section 4(1) and said it will include an expanded discussion of the terms "direct benefit and use" and "accomplishing a public purpose of support or stimulation" in its revised guidance. OMB did express a reservation, however, about requiring a review of each transaction. OMB believes that for the vast bulk of assistance and procurement actions a transaction level review is not necessary and in its revised guidance will call for such reviews only for those transactions that require it. Although we recognize that most decisions on individual transactions will be routine in nature, particularly when the guidance is revised, we believe it will be difficult to identify those that are nonroutine without some review of each transaction.

HUD, Justice, and the Department of Transportation (DOT) disagreed with our interpretation of section 4(1). We believe that Justice misinterpreted our position by inferring that we were of the opinion that contracts are the only appropriate instruments for intermediary relationships. In our opinion, an assistance instrument is appropriate if the intermediary is authorized to be assisted and assistance is the nature of the relationship. This is the same basic view held by Justice and we therefore believe there is no real disagreement. HUD and DOT, however, have fundamental differences of opinion with our interpretation.

HUD disagrees with our position that assistance awards can only be made to intermediaries when they are statutorily authorized to receive such assistance. HUD basically espouses the view that in intermediary situations direct benefit and use occurs only when the Federal Government actually receives the product or service produced by the intermediary. If the product or service is delivered instead to a third party which is authorized to receive Federal assistance, HUD contends an assistance award can be made to the intermediary. We continue to disagree with this argument as explained on page 10 of this chapter. In addition, Justice's comments point out that the act's definition of "other recipient" supports our position. The act defines other recipient as a party "authorized to receive Federal assistance or procurement contracts * * * ." (Emphasis added.)

HUD goes on to recommend deferring issuance of our report until OMB's new guidance is completed. In that most agencies found our report useful, we believe that its issuance will contribute to improving OMB's guidance.

DOT believes that the "direct benefit and use of the Federal Government" language in section 4(1) has contributed to misuse of assistance instruments in procurement situations and believes that the language should be removed from the statute. In intermediary situations, DOT, similar to HUD, believes that the "direct benefit and use" language forces it to use grants or cooperative agreements unless the Federal Government is the direct recipient or user of an intermediary's product or services. Because DOT believes that transactions with intermediaries generally should be by contract, it has used section 4(2) of the act to require the use of contracts with intermediaries. Section 4(2) authorizes agencies to use contracts in specific instances where they determine the use of a type of contract is appropriate.

The basic thrust of DOT's argument is considered in our discussion of section 4(1) and we find no need to alter that presentation. As to DOT's contention that the act must be amended, we do not believe that is necessary. When section 4(1) is applied to the immediate relationship between the Federal Government and the recipient as we outline in this chapter, we find that section 4(1)

yields results consistent with the act's intent. What is needed is improved OMB guidance on the application of section 4(1) and more training of officials on how to apply the act. As noted above, OMB agrees with our interpretation of 4(1) and plans to revise its guidance accordingly. Section 4(2) is, in effect, a second line of defense which expresses congressional preferance for contracts in intermediary situations.

OMB agreed with our interpretation that section 7(a) of the act does not create new authority to make assistance awards independent of program legislation. OMB said it will include such a statement in its revised guidance. EPA also agreed with us on section 7(a) but pointed out that our draft report characterized EPA as disagreeing with our interpretation. We revised appropriate sections of this chapter to indicate that only certain EPA officials held a contrary opinion on the interpretation of section 7(a).

ACTION did not believe our interpretation of section 7(a) was persuasive. It commented that a reasonable interpretation of the legislative history can also support an opinion that section 7(a) allows agencies to use grants and cooperative agreements even where their program legislation only authorizes contracts, unless such legislation specifically prohibits such assistance activities. To the extent there is disagreement on the Congress' intent, ACTION believes clarification should come from the Congress rather than OMB.

Although we agree that section 7(a) allows an agency to use grants and cooperative agreements where it was previously restricted by program legislation to using contracts, this should only occur when the program legislation actually describes an assistance relationship. To permit agencies to use either of the instruments irrespective of program legislation would be inconsistent with the congressional purposes of providing criteria for, and promoting more uniformity in, the selection and use of contracts, grants, and cooperative agreements. For this reason and because OMB, which has statutory responsibility for issuing interpretative guidelines, also shares our view, we do not believe congressional clarification is required.

Distinguishing between grants and cooperative agreements

OMB agreed to clarify its guidance on the terms normal involvement, normal Federal stewardship, and substantial involvement. However, OMB, ACTION, and the Departments of the Interior and Energy expressed concern with our suggested interim program approach to better defining substantial involvement.

The four agencies generally believed our interim approach could be counterproductive because later OMB guidance or experience might cause agencies to reverse decisions based on that approach. The magnitude of changes that may occur is difficult to predict. We do not believe, however, that changes would be necessarily undesirable. Indeed, the Congress anticipated that an evolutionary process might be needed to refine the meaning of grants and cooperative agreements.

Interior also questioned our interim approach because it believes normal involvement will not be any easier to define than substantial involvement for a given program. We found that officials' inability to determine whether substantial involvement was present often stemmed from a lack of knowledge about how other programs operated. Our thinking in suggesting the interim approach is that officials usually do know what is normal involvement for their own programs. Basing decisions on what level of involvement occurs most frequently (or is normal) within the program is a more natural starting point for these officials than concentrating first on what constitutes substantial involvement, which is now basically undefined.

Energy and ACTION commented that under our interim approach a given recipient can receive different types of assistance instruments for different programs where the Federal involvement is essentially identical. We recognize this could occur, but we believe that such inconsistencies can also result from OMB's current guidance. We believe such inconsistencies can be reduced, however, by an agencywide analysis and comparison of program decisions. We therefore added material to the report to emphasize that program decisions should be reviewed at a policy level. This review would promote more uniformity by determining whether the normal level of involvement for a particular program is actually substantial compared to other programs within the agency. If so, that program would generally award cooperative agreements. This review procedure could be incorporated into the policy level review of program decisions currently required in OMB's guidance.

We recognized in offering our suggested approach that some inconsistencies would continue and some changes might be needed as more operating experience is gained. However, we perceived the need for agencies to have a more structured basis to distinguish among normal involvement, normal Federal stewardship, and substantial involvement. We therefore offered the interim approach as a suggestion and are pleased that OMB considered it constructive and will give it serious consideration.

DOT did not comment on the interim approach but rather took issue with the act's basic structure. It said the cooperative agreement category is not needed, is confusing, and only provides further opportunities for program officials to avoid procurement regulations. DOT believes the Congress should amend the act to

delete the cooperative agreement category. We disagree because revised guidance should help to eliminate confusion, reduce opportunities for avoiding the procurement system, and make the cooperative agreement a more meaningful category of assistance. DOT also suggested that the original purpose of the act can be more easily achieved by establishing subcategories of assistance similar to the subcategories that exist within procurement. We believe this is what the act in effect began to do by dividing the assistance system into the subcategories of grants and cooperative agreements. The Congress anticipated that further standard subcategories, such as loans and subsidies, would be established in the future.

Finally, OMB, Justice, and Energy disagreed with our recommendation that OMB's revised guidance should recognize that highly prescriptive pre-award conditions, even if they are not accompanied by close monitoring or operational involvement during performance, may constitute substantial involvement. They believe that these requirements must be accompanied by close monitoring or operational involvement after the award is signed. They hold this opinion, as OMB indicated, because "involvement during performance of an activity must actually occur during the performance period". In our opinion, when an agency includes highly prescriptive requirements in an award their effect on the recipient usually comes during performance. For example, we found that agencies sometimes write requirements into awards that condition future funding on the completion of specified activities within prescribed time frames. Through such requirements, an agency clearly influences the recipient's activities during an award period and, in our opinion, this may constitute substantial Federal involvement. Close monitoring for compliance may occur, but even without it, the recipient must comply or risk audit disallowances, funding reductions, or disqualification for future awards. Therefore, we continue to believe that highly prescriptive requirements, by themselves, are a potentially useful indicator of substantial involvement.

# CHAPTER 3

# STRONGER OMB AND AGENCY MANAGEMENT EFFORTS NEEDED TO IMPLEMENT THE ACT

The steps taken by OMB and Federal agencies to implement the act have not been totally effective. Enough effort has not been made to bring the act to the attention of Federal officials responsible for its implementation. Most of the Federal agencies we reviewed had issued guidelines implementing the act. But some agencies issued their guidelines late and several agencies have not issued final guidelines. Agencies also have not established effective mechanisms to insure that agency officials use the guidelines or apply them properly.

As a result, many Federal officials do not know of the act or have inadequate information to apply it. Other Federal officials are resisting the use of the act because they fear they must change the type of instrument used to the detriment of their programs. They believe these changes will disrupt relationships with their recipients and possibly cause some recipients to withdraw from their programs.

## THE CRITERIA OF THE ACT ARE FREQUENTLY NOT BEING USED

In many programs, the act's criteria are not being used to select the appropriate instruments. This is partially due to the interpretation problems discussed in chapter 2. Frequently, however, Federal program officials both in Washington and the regions were not aware of the act. Further, when agencies had published guidance, most regional officials we contacted were unaware of it. In some programs, Federal officials were aware of the act but were trying to be excluded from its coverage or were discouraging its use by regional officials.

### Federal and recipient officials frequently do not know of the act

Many Federal officials are not implementing the act because they do not know of it. Our telephone survey indicated that, Government-wide, responsible officials in an estimated 43 percent

of all programs did not know about the act. For the six largest agencies this percentage ranged from 37 to 63 percent. Although they did not know of the act, about 84 percent of these officials said that they do use one or more of the act's instruments. This is not surprising in that the terms contract and grant have been traditionally used to describe Federal financial relationships.

Federal regional officials and recipients of Federal aid we contacted were also generally unfamiliar or only slightly familiar with the criteria of the act or OMB's guidance. For example, in one region, of 30 officials we interviewed in nine agencies, 10 officials were not familiar with the act and 10 were only somewhat familiar.

We also made limited contacts with recipients of Federal aid. Like many of the Federal officials, they were generally unaware of the act or its provisions. During our survey work in 1979 in one State, none of the officials of six recipient agencies could discuss the act or its purposes. Officials of four of these six agencies had not even heard of the act. Recipient officials we interviewed in our detailed review work during 1980 also had limited knowledge of the act. When they were aware of the act some Federal officials and recipients of Federal awards wanted to know more about it and were concerned about how they would be affected by Federal decisions implementing the act.

Attempts to resist complying with the act

Some Federal officials are trying to exclude their programs from coverage of the act or are reluctant to use the act's criteria because unwanted changes in required instruments could occur. Federal officials believe that the changes will (1) cause recipients to discontinue participation in their programs, (2) complicate working relationships with recipients, and (3) increase the likelihood of lawsuits against the Federal Government.

Federal officials have not substantiated their concerns, however, and there is some evidence that their concerns are overstated. Although significant changes in types of instruments and practices are possible, experience is needed before a valid assessment of the act can be made. The act gave OMB authority to except transactions and programs from the act's coverage for those cases where harm can be demonstrated by Federal agencies. Bills to extend this authority, which lapsed in March 1981, are being considered in the Congress.

Attempts to be excluded from coverage of the act

Officials in several agencies expressed concern that compliance with the act would cause recipients to discontinue participation in their programs. For example, Social Security Administration

(SSA) officials sought and obtained legislation they believe excludes the Disability Insurance program from the act's coverage. The Disability Insurance program utilizes States to make determinations of eligibility for Federal disability insurance payments. Officials said they were not willing to use contracts with the States because, in their view, States would not accept contracts and would drop out of the program. If the States drop out the Federal Government would, by law, have to make the disability determinations with Federal personnel.

Presently, SSA enters into agreements with the States but does not strictly follow procurement or assistance rules and procedures. SSA officials are aware that the relationship with States under the Disability Insurance program is not one of assistance, but rather a purchase of services. Their concern about States' participation is based on States' resistance to agreements developed by SSA which were intended to clarify roles and responsibilities. One SSA official said the States were not willing to accept the added controls, several of which were procurement clauses, in the new agreements. According to SSA statistics, 21 of the States, as of June 1980, have signed these new agreements.

Even before SSA obtained the apparent legislative exemption, SSA officials said they did not plan to implement the act. Because of SSA's plans not to implement the act, we contacted OMB to determine whether an exemption had been granted. An OMB staff member told us that SSA had not been granted an exemption and should classify these agreements as contracts, cooperative agreements, or grants. After SSA officials said they had the legislative exemption, we again contacted OMB. OMB officials did not know that SSA had sought a legislative exemption, and they had not taken action to resolve this matter with SSA.

The Department of Agriculture's Forest Service is currently preparing draft legislation that would create a new class of transactions for its programs. A Forest Service official said that in the interim the Service has moved to implement the act and is now using procurement contracts for many transactions it previously entered into with cooperative agreements but which no longer meet the act's definition of cooperative agreements. This official said, however, that recipients are unhappy with the contracts because they must comply with procurement regulations and requirements. He said some States claimed their laws prohibit them from accepting contracts. This official acknowledged that the Forest Service has not verified the States' claim but has nevertheless requested an OMB exemption. An OMB official said that the office had not granted an exemption to the Forest Service upon its original request, because data submitted by the Forest Service did not support its claim that exemptions are needed. OMB, however, told the Forest Service to use existing agreements in three programs while discussions continued on those programs.

Federal officials have not clearly substantiated that contracts cannot be used. There is some contrary evidence available to indicate that States and local governments will accept contracts. For example, the Department of Labor, in its Job Corps Program, now uses some performance-based contracts with States instead of grants. Under this type of contract, payment is made by Labor for each person recruited under the Job Corps program. Labor officials said they switched to a performance contract because State and local governments were not performing adequately under the cost reimbursement grant. According to Labor officials, the cost per enrollee dropped dramatically after they switched to performance contracts, and only a few States refuse to accept a contract. At the time of our review, Labor had not pressed the matter with these States and continued to award grants.

Limits on officials' authority to select instruments

Although not attempting to be excluded from the act's coverage, other program officials have similar reservations about using instruments required by the act. In an attempt to minimize perceived problems, Federal agencies do not always allow officials making an award to choose the type of instrument required by the act. In other words, agency officials are sometimes required to use one type of instrument when another type may be more appropriate.

Unless transactions are reviewed on a case-by-case basis, there is little assurance that the instrument selected meets the criteria of the act. For example, where a program has both procurement and assistance authority, each transaction must be reviewed to insure that it has been designated properly. As described in chapter 2, Federal officials must determine the purpose and characteristics of each transaction, whether authority exists to issue an assistance award, and how much involvement is contemplated for each recipient. The extent of involvement often varies within programs depending on the recipient, indicating the need for case-by-case decisions on whether a grant or cooperative agreement is most appropriate.

In spite of this need to decide between different types of instruments, many regional officials told us they do not have the authority to determine what instruments are appropriate for given transactions. Although agencies' implementing guidelines may not specifically restrict their authority, regional officials told us that restrictions occur through headquarters interpretations of the guidance or decisions that a certain type of instrument will be used on a programwide basis. This is sometimes deliberately done to discourage the use of cooperative agreements. For example, an EPA headquarters program official was concerned that a change to a cooperative agreement could cause confusion on the part of recipients. Although he recognized the program should use cooperative agreements, the official said he did not want mayors throughout the nation upset because of a name change in the award. EPA

finally decided to permit the use of both grants and cooperative agreements, but a regional official said he understood only grants are to be used. Similarly, CSA headquarters officials were concerned that their regional officials might use cooperative agreements to gain more control over recipients than might be appropriate and therefore sought to limit regional officials knowledge of the act and thus discourage them from using cooperative agreements. We believe regional officials should be informed of any agency policies, and how they should be applied in order to effectively implement them.

In the case of HUD and Labor, regional officials who had heard about the act and requested headquarters guidance were advised not to take any action or be concerned about the act.

Fears of liability under a cooperative agreement

Many Federal officials are also reluctant to use cooperative agreements because they fear these agreements may increase the likelihood of lawsuits against the Federal Government. This fear is based on their belief that if the Government is substantially involved with the recipient, the courts may consider the Federal Government to be partially responsible for the recipient's actions.

In its letter commenting on OMB's draft guidelines, the Department of Transportation's Urban Mass Transportation Administration (UMTA) expressed concern that characterizing programs as "cooperative agreements" might expose the Department to tort claims for the negligence of recipients engaged in UMTA projects. UMTA is apprehensive about this point because it believes a cooperative agreement could possibly be interpreted as a joint venture with liability shared by both parties.

Court decisions generally have not held that the Federal Government is liable for the actions of recipients of Federal assistance. The courts have held that although Federal funds are awarded to cover some or all of the costs of recipients' projects, the projects themselves are considered to be the recipients' and their direction and operation are the recipients' responsibility.

A 1976 Supreme Court case, United States v. Orleans, 425 U.S. 807 (1976), suggests that the Government may transform a normal relationship with an independent grantee into an agency relationship through the exercise of very close day-to-day Federal supervision of the grantee. If a grantee is an agent of the Federal Government, the Government may be financially responsible for the agent's conduct. Although the Court has yet to find that a Federal grantee is an agent of the Government, the suggestion has produced a number of lower court cases where the argument has been made.

Courts, however, may be reluctant to allow the statement in Orleans to become a means by which Federal officials can change

the nature of the congressionally authorized relationship through excessive zeal in day-to-day supervision. In practice, the rule may well develop that no matter how far Federal employees go in supervising grantee activities, an agency reltionship is not created unless expressly authorized by the program legislation because

--it cannot be shown that the grantee had to accept the offending supervision under the terms and conditions of the award; and

--if the relationship contains such elements of supervision as to make the grantee an agent, it exceeds the agency's program authority and accordingly cannot bind the Government.

So far, lower courts have also rejected the notion that the Government might be subject to direct tort liability for acts of a grantee because of some shortcoming in the way the Government has exercised its program responsibilities over assistance programs. Ultimately, other theories may raise a more substantial danger of increased Government liability than the agency theory, where Government employees participate directly in collaborative-type cooperative agreements. It seems possible that under some facts where there is a combination of an instrument called "cooperative agreement" and a Government employee actually participating in the project activity the Government may be held liable with a grantee.

We do not believe that the Congress intended that substantial involvement in cooperative agreements would normally reach the point of sharing responsiblity. The report of the Commission on Government Procurement explained that the cooperative agreement category was not intended to establish a new assistance relationship, but rather to divide the range of grant-type activities into two more descriptive categories.

OMB's guidelines note that Federal agencies' statements of anticipated substantial involvement "must be developed with care to avoid unnecessarily increasing Federal liability under the assistance instrument." We believe this guidance should be expanded to reflect the issues that are developing in the courts and to emphasize that the act itself does not authorize agencies to impose controls inconsistent with their authorizing legislation.

## AGENCIES NEED TO ESTABLISH BETTER IMPLEMENTATION SYSTEMS

Under OMB's leadership, Federal agencies are responsible for insuring that the act's criteria are observed in administering their programs. Federal agencies, however, have not always taken timely or effective steps to develop and distribute internal guidance and insure that it was acted on.

## Agency efforts to provide internal guidance and training have not been timely or effective

OMB issued guidelines implementing the act on August 18, 1978. However, agencies have not issued internal guidelines in a timely fashion or provided adequate training to their staffs. As of August 1980, 4 of the 10 agencies we reviewed had not issued final guidelines, and 2 other agencies had not issued guidelines until early 1980. As previously noted, our mid-1980 questionnaire showed that about 43 percent of headquarters program officials did not know of the act. The status of the 10 agencies' guidance as of August 1980, is shown below.

| Status | Number of agencies |
|---|---|
| Final in 1978 | 2 |
| Final in 1979 | 2 |
| Final in 1980 | 2 |
| Draft in August, 1980 (see note a) | 4 |
| Total | 10 |

a/Includes one agency's temporary guidance, which expired without being finalized.

Agency guidance was issued late or has not been issued for several reasons. Some agencies simply did not move in an expeditious manner. In one agency for example, policy officials said draft guidelines "just sat" in the Office of General Counsel for about 7 or 8 months. These officials had earlier indicated to us that the guidelines did not have a high priority with them. In other agencies there was internal disagreement over the guidelines, and/or personnel assigned to work on implementing the act were reassigned to other duties or left their agencies.

Where agencies had issued guidance, Federal officials responsible for implementing the act did not always have knowledge or copies of their agencies' guidelines. For example, in April 1980, regional and headquarters officials of one agency had not received agency guidelines which had been issued in January 1980. In another agency, the region had received and filed the guidelines but regional officials were not aware of them at the time of our visit. These officials subsequently told us the guidelines had been put into a general file and no action was taken because no one was assigned responsibility for their implementation. A somewhat similar situation occurred in the regional office of another agency. In a regional office of a fourth agency, agency guidelines

were not being followed because most agency officials we contacted were not knowledgeable about the act.

Agencies have held some training sessions on the act, but their effectiveness is questionable. Early in 1980, a year after implementation of the act was to be fully underway, most of the 10 agencies we reviewed had held few formal training sessions on the act. The training that had occurred was usually informal, constituted a general introduction to the act, and was not conducted agencywide. Only two agencies planned additional training efforts. Despite the training that had been offered, as noted earlier, our mid-1980 telephone questionnaire and work in two regions indicated that officials in many programs did not know of the act, or wanted additional guidance.

This lack of effective guidance and training may also partially explain why, on the basis of the results of our questionnaire, responsible officials in about 86 programs who knew of the act said they have no plans to implement it. Most of these officials believed the act did not apply to their programs. However, on the basis of our questionnaire, we estimate that 70 percent of the programs use at least one of the act's instruments, and about one-third of the programs use two or more of the act's instruments.

## Effective agencywide oversight of implementation is lacking

In its guidance, OMB noted that the act was a preliminary step toward the long-range overhaul of Federal assistance activities and advised agencies they should anticipate extensive questions about the effects of implementing the sections of the act dealing with the criteria for using contracts, grants, and cooperative agreements. Accordingly, OMB instructed agencies to develop systems of records that would allow them to answer questions such as the number and type of award instruments used, classes of recipients, criteria for determining which instruments to use, and experiences and problems in implementing the act. OMB also noted that the determinations of whether a program is principally one of procurement or assistance and whether substantial Federal involvement will normally occur are basic agency policy decisions, and agency heads should insure that the general decisions for each program are made or reviewed at a policy level. OMB also asked agencies to designate liaison officials to serve as focal points on matters concerning the act.

All of the 10 agencies we reviewed designated liaisons as requested by OMB. Most of them also either already had or subsequently established assistance policy offices to which these officials were assigned. However, most offices either lacked the authority, inclination, or staff to oversee and assess the act's implementation.

In 6 of the 10 agencies we reviewed, the assistance policy offices did not, in our opinion, have adequate authority or staff to insure that implementation would be consistent or adequate. Officials in one agency, for example, noted that although the program offices must, according to policy, comply with guidance issued by the assistance policy office, they are in practice very autonomous. One official of this agency told us that his office was consistently unable to resolve disputes with program offices. This same official also noted that due to a lack of staff, he is unable to even review the additional guidance that these offices publish.

In another agency there was evidence that top officials have not given adequate support to the assistance policy office. Agency officials note that although the agency's 62 assistance programs account for close to, if not more than, half the agency's annual expenditures, there is only one staff person responsible for agencywide assistance policy. They said the agency has a bias toward procurement and has not provided adequate support for assistance management. These officials said no effort is made to oversee implementation of assistance policies. In a third agency, a centralized assistance policy function has only recently been established. A fourth agency does not have an office responsible for agencywide assistance policy development and oversight.

It is debatable whether program decisions were made or reviewed at a policy level as required by OMB. We encountered difficulties in determining who made the decisions and on what basis they were made. It is clear, however, that virtually none of the 10 agencies we reviewed had placed significant emphasis on systematically gathering information in anticipation of future questioning and monitoring how the act was being implemented. To the extent agencies had monitored implementation, it was usually on an informal, ad hoc basis. Officials often indicated it was too early to monitor implementation or that they lacked staff to undertake such work.

The lack of data gathering and monitoring has prevented agencies from identifying whether and how their guidance was being used and whether decisions were properly made and documented.

## OMB OVERSIGHT OF AGENCY IMPLEMENTATION OF THE ACT SHOULD BE STRENGTHENED

OMB must rely on Federal agencies to implement the act but has not developed a systematic approach to determine the extent to which the act is being applied to Federal programs. Over time, it has become apparent that proper implementation of the act is heavily dependent on OMB oversight. As discussed in chapter 2, the act's criteria and OMB's guidelines are being interpreted in divergent ways. Some oversight by OMB has occurred, and in its report to the Congress required by section 8 of the act, OMB indicates that more investigation into the act's implementation is needed.

However, in fulfilling its commitment, we believe OMB needs to devote more attention to the manner in which it oversees agency implementation and the way that it responds to issues brought to its attention.

OMB has primarily overseen the act's implementation on an informal, ad hoc basis. To detect implementation problems it has relied extensively on discussions with agencies' liaisons and periodic contacts with other officials. The principal OMB effort to systematically gather data on the act's implementation occurred in connection with the study required by section 8 of the act. OMB required agencies to answer, by March 1, 1979, a series of questions concerning their experience in implementing the act. However, many agencies did not respond, and, because agencies had limited experience with the act, the answers from those that did respond were limited in scope and completeness.

With its limited monitoring, OMB did identify several issues requiring its attention. However, more monitoring is required to systematically identify and resolve implementation problems. During our early review work we advised OMB of inconsistencies in agencies' policies and proposed practices concerning assistance awards to profitmaking firms, payment of fees, competition, and certain provisions in its guidance. Some agency officials had detected similar inconsistencies. Accordingly, OMB is now developing new guidance on several of these issues and plans to further investigate the act's implementation.

However, OMB does not believe it has sufficient authority to issue legally binding interpretations of the act. Currently, OMB is authorized by the act to issue supplementary interpretive guidelines. According to OMB, Federal agencies have questioned whether such interpretations are binding. To rectify this perceived problem, in its 1980 report OMB proposed to strengthen the act, to provide OMB specific authority to issue implementing regulations. In our opinion, the Congress clearly intended that OMB direct Federal agencies' actions. Senate Report 95-449 states that the act gives the OMB Director authority "to issue Government-wide guidance and to manage agency implementation of the requirements of this Act." (Emphasis added.)

Although the informal procedures used thus far have identified some issues, other issues have not been adequately identified and resolved. In particular, OMB officials need better information on whether and how agencies are implementing the act. For example, OMB was not aware that two agencies are taking steps to amend program legislation to remove several programs from coverage of the act. OMB officials said they have no way to know what agencies are planning to do in such cases. They said it is especially difficult to monitor appropriation legislation because of time constraints. Although made aware of this matter, OMB has not yet followed up to determine the appropriateness of the agencies' actions.

The need for closer OMB monitoring of how agencies are implementing the act is also supported by indications that some agencies may utilize cooperative agreements in unique ways. For example, EPA believes that the Congress intended for agencies to experiment with cooperative agreements. The Department of Energy plans to utilize cooperative agreements in a unique way by combining procurement and assistance terms and conditions in individual transactions in order to use procurement controls in an assistance environment. Although the cooperative agreement instrument is still evolving, we believe OMB needs to continually review its application to help insure that the act's goal of uniformity is not lost and that clear differences are maintained between procurement and assistance instruments.

OMB also needs to improve its means for documenting and responding to problems identified through its monitoring activities. While it has been relying on informal procedures for reviewing implementation, OMB has not kept a record of issues raised in discussions with Federal officials nor has it systematically communicated any verbal guidance given in individual cases so that other agencies might benefit. For example, OMB has provided some Federal agencies with interpretations of its guidance on substantial involvement, section 7(a), and intermediary transactions, but it has not issued supplementary guidance to other agencies which also can be affected by its interpretations and policy decisions.

Finally, OMB's ability to adequately monitor the act's implementation may be constrained by staff availability. Administration of OMB's guidelines rests with a small staff of four professionals whose work has been basically confined to the OMB study and many followup projects to develop new OMB policies. OMB supplemented this permanent staff with personnel from Federal agencies to help conduct these activities. Because of turnover in agency details, this temporary staff may not be suitable for long-term monitoring efforts. Although we did not evaluate the adequacy of OMB's staffing, we believe that more effort is needed in monitoring implementation of the act.

## OMB'S AUTHORITY TO EXCEPT PROGRAMS WAS BENEFICIAL AND SHOULD BE RENEWED

The Congress, recognizing that problems might arise in applying the act to the many and diverse Federal programs, authorized the Director, OMB, to except transactions or programs from the act. This authority, contained in section 10(d), expired in March 1981.

OMB used the authority with restraint in the 3 years it was available, excepting only the general revenue sharing and countercyclical aid programs and nonmonetary grants. Requests for exceptions, although infrequent, have involved significant issues and

were carefully reviewed. For example, had general revenue sharing been subject to the act's provisions and classified as a grant, the attendant requirements and procedures would have been counter to congressional intent on how the program should operate. Because the act has not yet been applied in a great many programs, we anticipate that additional cases will arise in which the exception authority would be useful.

Other considerations also argue for renewing the authority. A principal purpose of the act is to promote uniformity in the use of grants, cooperative agreements, and contracts. Although there have been numerous difficulties, as explained earlier, in achieving this purpose, section 10(d) promoted greater consistency, since it essentially empowered OMB to be the final arbiter on implementation of the act. Future requests for exceptions might highlight other problems with both the OMB guidance and the act by providing actual case examples demonstrating how agencies apply OMB's guidance. Finally, reviewing the requested exceptions could assist the Congress and OMB in judging whether the act needs clarification or whether it is being properly interpreted by executive agencies.

OMB recognizes that the exception authority was useful and has requested congressional renewal of the authority. Bills have been introduced in both the Senate and House which would renew this authority.

## CONCLUSIONS

OMB and Federal agencies have not aggressively implemented the act. The administrative systems needed to achieve the act's objectives have not been established. OMB provided implementing guidance to Federal agencies but has not actively monitored its use. Among Federal agencies, steps to implement and administer the act have not always been timely or effective.

Many Federal officials have insufficient information on how to meet the objectives of the act. Frequently, the act's criteria are not being used when decisions are made to use grants, cooperative agreements, or contracts to award Federal funds. This is due in part to the problems discussed in chapter 2. It also indicates, however, the need for more training on the application of the act and OMB's guidance.

Federal agencies have not placed a high priority on implementing the act. Internal guidance and efforts to oversee the act's implementation have been limited. From the perspective of some Federal officials there are disincentives to implementing the act, such as disrupting ongoing relationships with grantees and increasing the likelihood of lawsuits against the Federal Government.

If the objectives of the act are to be attained, OMB and Federal agencies need to place increased emphasis on the administration of the act. Both need to establish better coordination and oversight mechanisms to ensure that officials' awareness of the act is increased, that variant practices and procedures are identified and resolved, and that policies conform with the objectives of the act.

Implementation of the act would also be facilitated by renewing the OMB exception authority previously provided by section 10(d). Until the authority expired in March 1981, OMB used it judiciously. Continued exception authority would be beneficial in (1) acting as a safety mechanism when application of the act's provisions might not be practical, (2) promoting consistent use of the act's instruments, and (3) providing both the Congress and OMB useful information for assessing implementation of the act and OMB's guidance.

## RECOMMENDATION TO THE CONGRESS

In order to accommodate potential unanticipated consequences from the act's use and to facilitate consistent implementation, we recommend that the Congress renew, without time limit, OMB's authority to except individual programs or transactions from the act's provisions.

## RECOMMENDATIONS TO THE DIRECTOR, OMB

To improve the administration and monitoring of the act, we recommend that the Director, OMB:

--Direct Federal agencies to (1) develop administrative systems necessary to implement and monitor compliance with the act, (2) identify emerging problems so that revisions to policies and procedures can be considered, (3) provide adequate staff training and technical assistance on the act and OMB guidelines, and (4) develop systems of records on their operating experiences in implementing the act.

--Actively monitor the implementation by Federal agencies to assure that OMB policies and guidelines are carried out uniformly and in a timely manner.

--Establish an effective, ongoing system to document and respond to problems identified during monitoring activities.

--Revise the OMB guidance to provide more insight into how agencies can avoid unnecessarily increasing Federal liability under cooperative agreements.

## AGENCY COMMENTS AND OUR EVALUATION

OMB agreed in a general sense that the executive branch must improve management of all requirements which are generally applicable to assistance programs. Because the Federal Grant and Cooperative Agreement Act is but one of approximately 60 such requirements, OMB plans to address the problems we identified as part of a broader effort with primary emphasis on helping Federal agencies to better manage themselves. Accordingly, it will soon issue a new OMB circular on general assistance policies and include the revised guidance on the act as an attachment.

OMB's planned approach is a positive response to our recommendation and should foster better management of Federal assistance programs. We agree with OMB that the responsibility for good management must rest with the assistance agencies and that many of the problems can be resolved by agencies themselves once their internal management systems are developed to the point that they are routinely used. We believe, however, that OMB still needs to adopt a more active monitoring role.

The Department of Energy expressed some reservations about the need for more OMB oversight of the act's implementation. Energy officials believe that increased oversight will be of little value until better guidance is published and, conversely, with better guidance there will be less need for OMB oversight. We continue to believe that more oversight is needed. As pointed out in chapter 2, OMB's guidance is still evolving. In the interim, monitoring will (1) enable OMB to gather the data needed for periodic revisions and (2) help promote the uniformity in use of grants, cooperative agreements, and contracts envisioned by the Congress.

ACTION was concerned that developing adequate administrative and monitoring mechanisms for implementing the act would increase the regulatory and paperwork burdens on Federal agencies. We recognize that some increase in burden may result, but we do not believe that the increase needs to be substantial. More importantly, we believe the virtual absence of any administrative and monitoring systems that we found in some agencies must be rectified if the act is to be adequately implemented.

Finally, OMB agreed to revise its guidance to provide more insight into how agencies can avoid unnecessarily increasing Federal liability under cooperative agreements.

# CHAPTER 4

## NEED TO DEVELOP DIFFERENCES IN OPERATING PROCEDURES FOR GRANTS, COOPERATIVE AGREEMENTS, AND CONTRACTS

The Federal Grant and Cooperative Agreement Act was intended to do more than provide standard criteria to help ensure the proper selection of contracts, grants, and cooperative agreements. In passing the act, the Congress also envisioned (1) a reduction in unnecessary administrative requirements in Federal assistance programs, (2) a better understanding of Federal and recipient roles and responsibilities under the various types of relationships covered by the act, and (3) improvements in the management and oversight of Federal assistance programs. These purposes are not likely to be realized without further efforts to make the act's distinctions more meaningful and to utilize the act more fully in reforming the assistance system.

The purposes of the act will be advanced through improved guidance and management procedures as discussed in the preceding chapters. Choices among contracts, grants, and cooperative agreements must have discernable consequences in operating procedures, if the choices are to be meaningful. However, the consequences of selecting between instruments are often not clearly known. Currently, there are differences between the procedures for procurement contracts and assistance agreements, although these differences seem to be gradually eroding. In the assistance arena, no such obvious difference exists between grants and cooperative agreements. To many officials, the choice constitutes a distinction without a difference in terms of operating procedures.

If operational distinctions are developed (1) Federal officials will have more incentive to select the appropriate instrument, (2) the instrument choice will better facilitate communicating the respective roles and responsibilities of the Federal Government and recipients, and (3) the Congress and executive agencies should be better able to oversee the implementation of Federal programs.

### DIFFERENCES BETWEEN PROCUREMENT AND ASSISTANCE PROCEDURES APPEAR TO BE ERODING

Different laws, regulations, and procedures apply to procurement contracts and assistance awards. However, these differences are eroding as Federal officials turn to procurement for precedents to apply in assistance awards. This will continue until a decision is made as to the extent and nature of the differences that should exist between procurement and assistance.

Because the Congress perceived that the Government's purpose is different in a procurement relationship from an assistance relationship, it clearly intended that the requirements associated with these two basic relationships would also differ. For instance, Senate Report 95-449 noted that one effect of the act would be:

> "When an agency, complying with the criteria established herein, changed the award mechanism for a particular activity from a type of grant to a type of procurement contract, then the procurement regulations would apply. Conversely, when an agency changed the award mechanism from a type of procurement contract to a type of grant, the regulations and statutes applying to procurement contracts would no longer apply. The regulations and statutes applying to transactions of Federal assistance would apply."

The differing requirements for procurement contracts and Federal assistance awards exist in statutes, regulations, and OMB guidance. For example:

--Procurement contracts are subject to some laws which either are not applicable to assistance awards, e.g., the Service Contract Act and Small Business Investment Act as amended; or laws which are not usually applied to assistance, e.g., Buy American Act and Walsh-Healey Act. Conversely, assistance awards are sometimes covered by acts which do not apply to procurement contracts, e.g., the Joint Funding Simplification Act, and the Intergovernmental Cooperation Act of 1968 (excluding Title V).

--Procurement contracts are subject to the Federal Procurement Regulations or Defense Acquisition Regulations. Assistance awards are not subject to these regulations nor is there a cohesive body of regulations covering assistance.

--Procurement contracts are subject to some OMB circulars which are not applicable to assistance awards, e.g., A-109, Major Systems Acquisitions, and A-76, Policies For Acquiring Commercial Or Industrial Products and Services for Government Use. Conversely, assistance awards are subject to some circulars which do not apply to Federal procurement awards, e.g., A-102, Uniform Administrative Requirements For Grants-in-aid to State and Local Governments.

The overall differences between the requirements governing procurement contracts and assistance awards nevertheless seem to be decreasing as Federal officials sometimes turn to the precedents of the procurement system when

--selecting clauses to be included in assistance award documents;

--designing competitive procedures for assistance awards;

--establishing procedures to debar recipients who have not performed well in the past from receiving future Federal awards; or

--resolving disputes under agencies' internal procedures, under GAO's bid protest procedures, and in the courts.

The convergence of procurement and assistance rules and regulations has also flowed from the increasing use of both to achieve social or economic goals. During the explosive growth of assistance programs over the past three decades, the Congress and Presidents have attached requirements promoting social or economic goals to both systems. For example, the Davis-Bacon Act, which applied originally to construction work under Federal contracts, has been applied by the Congress through program statutes to construction under various Federal assistance programs. Similarly, Executive Order No. 11246 on discrimination due to race, color, religion, sex, or national origin, applies to both procurement and financial assistance programs.

The procurement and assistance systems should not become fully overlapping. We believe that the characteristics of Federal assistance relationships fundamentally differ from those of procurement relationships and, accordingly, it would be inappropriate to have one system of requirements that does not adequately provide for different treatment of the two relationships. Further, if the two systems converge, there will be less incentive to choose the appropriate instrument as required by the act because the choice would have few practical consequences. A lack of practical consequences flowing from the choice of instrument would also defeat the act's purpose of having each type of instrument clearly reflect the kind of relationship intended. Executive branch officials, who are responsible for assistance policy, have also expressed concern about excessive overlap of the two systems or inappropriate use of procurement principles in assistance relationships.

An example of where assistance procedures should differ from procurement is the power to terminate for the convenience of the Federal Government. In procurement, when a situation changes so as to nullify the Government's need for the product or service, the Government has the option of terminating all or part of the contract before its agreed upon completion and making a reasonable settlement with the contractor. In assistance relationships, the Federal Government's and the recipient's interests coincide. Accordingly, a similar option would not seem appropriate without specific restrictions. Although the Government may change its objectives, it would not seem appropriate that it have an unrestricted power to unilaterally terminate what was intended to be a project of mutual interest.

If terminations for Federal convenience are permitted in assistance, restricting them to the ends of funding periods would allow for more orderly transitions in which the assisted recipient could either find other resources or phase down its activities over time. Nevertheless, some Federal officials feel a need to be able to terminate for convenience in assistance programs, and provisions for unilateral Federal terminations appear in assistance guidance or actual assistance award documents.

Identifying what differences should exist between the two systems will be difficult because some elements of procurement can be reasonably applied to assistance. For example, assistance agreements have long been recognized by the courts and the Comptroller General as forming a type of contractual relationship between the Federal Government and the recipient. Therefore, certain principles or practices that have been developed under procurement law would seem appropriate for application in total or a slightly modified form to assistance relationships.

The Federal purpose in the relationship should be the key to determining which features should be unique to each system, or how the same overall feature might differ in scope or emphasis depending upon the system to which it is applied. The purpose in procurement, to acquire something, leads to rules and regulations which are designed to protect and promote the Federal interest while allowing the potential contractor a fair opportunity to compete and, where profits are permitted, a reasonable profit. The purpose of assistance relationships is to support or stimulate a recipient so that it can carry out an activity coinciding with a Federal statutory objective. The common interest of the Federal Government and the recipient in achieving an objective should therefore be reflected in assistance roles and regulations.

## DIFFERENCES BETWEEN GRANTS AND COOPERATIVE AGREEMENTS NEED TO BE ESTABLISHED

Currently there are no standard operational differences between grants and cooperative agreements. The potential utility of these classifications cannot be fully realized until operational differences are established. The lack of operational differences is primarily due to the newness of the cooperative agreement instrument to most agencies, to the equal application of OMB circulars to both grants and cooperative agreements, and to the lack of knowledge of the full range and diversity of agency involvement with recipients.

The operational consequences of choosing a grant or a cooperative agreement are presently so unclear that some officials consider the choice to be a distinction without a difference. Officials ranging in responsibility from those establishing agencywide assistance policies for hundreds of programs to those associated

with individual programs have expressed sentiments that the grant versus cooperative agreement choice has no practical impact. However, some of these officials nevertheless do foresee potential benefits if meaningful distinctions were made. For instance, some officials believe that if the grant versus cooperative agreement choice were made meaningful, then both the Congress and agencies could make more intelligent analyses and decisions about how programs are and should be operating.

As discussed in chapter 2, Federal officials do not understand how to identify or use a cooperative agreement. The act took what used to be a very broad category of assistance relationships, known as grants or grants-in-aid, and divided it into two subsets--grants and cooperative agreements. Although cooperative agreement relationships--assistance relationships where the Federal Government was substantially involved with recipients--had been present in agencies, they had not been systematically identified as such nor were they administered under a separate set of rules and procedures.

OMB's decision to apply Circulars A-102 and A-110 to both grants and cooperative agreements was ultimately based on a passage in the act's legislative history which implied that it should apply the circulars to both instruments. These two circulars establish uniform financial and other administrative requirements for grants-in-aid to State and local governments and for grants and agreements with institutions of higher education, hospitals, and other nonprofit organizations, respectively. We believe that the Congress intended that the circulars be applied to both instruments as an interim measure while improved guidance was being developed. In conducting the study required by section 8 of the act, OMB did leave open the possibility of building upon existing guidance; however, it did not produce such revised Government-wide guidance.

Many officials believe that OMB's decision to apply Circulars A-102 and A-110 to both grants and cooperative agreements significantly limits the ability to create operational differences between the instruments. HHS officials, for example, believe that because the circulars prescribe uniform administrative requirements and constrain agencies from expanding the requirements, applying them to cooperative agreements limits potential Federal involvement in a recipient's administration of an award. Consequently, these officials conclude that the ability to be substantially involved is restricted to matters relating to the program itself, such as who is to be served and how. But Federal officials often reason that they still need an ability to vary reporting and financial controls.

Federal officials' perception that these circulars effectively limit their ability to create operational differences between grants and cooperative agreements are not entirely accurate. Both circulars allow some variability in how agencies can treat their recipients. The broadest allowance for variability exists under

the circulars' Exceptions for certain recipients provisions. The exceptions provide that:

> "if an applicant/recipient has a history of poor performance, is not financially stable, or its management system does not meet the standards prescribed in the Circular, Federal agencies may impose additional requirements as needed provided that such applicant/recipient is notified in writing as to:
>
> (a) Why the additional standards are being imposed;
>
> (b) What corrective action is needed."

When exercising the exception, agencies do not need to obtain prior approval from OMB but must send a copy of the recipient notification letter to OMB.

Although some of the circulars' provisions afford the opportunity for variations on the basis of whether a grant or cooperative agreement is being used, we believe the circulars should be revised to establish clear operational differences for grants and cooperative agreements. Within OMB there is some sentiment that developing separate terms and conditions for each type of instrument may be desirable, but an agency decision on this has not been made.

As an approach to restructuring the circulars, we would suggest that the provisions be analyzed to identify (1) minimum requirements for each guidance provision, such as closeout procedures or frequency of financial reports, (2) optional requirements above the minimum, but still consistent with a grant relationship, and (3) requirements above those available in grants that are consistent with and can only be used in a cooperative agreement relationship. Under this structure, the optional requirements for both grants and cooperative agreements would be available only when program officials judge they are needed and would better express the nature of Federal involvement. Some hypothetical revisions to A-102 and A-110 are illustrated in the table on page 57.

Attachments H of A-102 and G of A-110, which provide for uniform financial reporting requirements, specify that financial reports are not to be required more than quarterly or less than annually. In a hypothetical restructuring of this guidance provision, the "not less than annually" provision could be viewed as the minimum considered necessary for adequate Federal stewardship. The provision allowing up to quarterly reports provides a range of normal reporting requirements that could also be permitted in grant relationships. In situations where a recipient has not properly accounted for Federal funds from prior awards or is a new recipient that the agency wishes to assist in establishing a good

## Hypothetical Revision To Selected A-102 And A-110 Provisions

| | Financial reports (frequency) | Financial reports (contents) | Records retention (note a) | Monitoring (frequency) | Closeout |
|---|---|---|---|---|---|
| **Grant Provisions** | | | | | |
| Minimum requirements | 1 Annually | Specific, nonwaivable financial information requirements, e.g., figures showing current status of funds | As specified in A-102 or A-110 | 0 to 1 Annually | Standard closeout procedures including suspension and termination for cause or mutual convenience |
| Optional requirements | Quarterly | Certain additional financial information requirements compatible with a grant relationship, e.g., projected future cash need | None | Quarterly | Same as minimum |
| **Cooperative Agreement Provisions** | | | | | |
| Optional requirements | Monthly | Specified financial information requirements beyond those available for grants, e.g., copies of vouchers | None | Continuous presence | Minimum plus a restricted termination for Federal convenience |

a/Here the minimum requirement effectively sets a maximum for any type of instrument.



MICROFILMED FROM BEST AVAILABLE COPY

accounting process for the Federal funds, an agency might want to obtain financial reports on a monthly basis. Since an agency would want these monthly reports because it determines more involvement with the recipient is needed, requiring financial reports more frequently than quarterly might be a logical option available only under cooperative agreements. Finally, even under cooperative agreements, to insure against an unreasonable frequency of reports an absolute maximum of monthly reporting could be established which could not be exceeded without OMB approval.

Just as the guidance on frequency of financial reports could be modified to coincide with the act, so could the guidance on the contents of reports. Attachments H and G of A-102 and A-110, respectively, also specify, through a set of standard reporting forms, what financial information can be obtained from recipients. However, not all of the information on the reports has to be collected since agencies can waive information requirements if deemed unnecessary for decisionmaking. These permissible information requirements could be rewritten to specify which financial information requirements could never be waived, that is, are the minimum necessary for prudent stewardship. The rest of the currently allowable financial information requirements on the standard forms might then also be available under grant relationships. Finally, requiring information beyond that on the standard forms could be designated as an option available only when needed and only under cooperative agreements.

A third guidance provision that could be restructured to parallel the act's provisions is the frequency of monitoring visits. Both A-102 and A-110 provide that Federal awarding agencies shall make site visits as frequently as practicable. This broad charge could be revised to provide that, as a minimum, an agency can make either no visit or one visit per year. No visits might be acceptable when a recipient is highly capable, or the dollar award is very small. At the next level, yet still consistent with a grant relationship, up to quarterly visits might be deemed appropriate. Lastly, site visits more frequent than quarterly would be conducted only in cooperative agreement relationships. This option might be frequently used when the Federal agency collaborates with a recipient in the conduct of a project such as in scientific research.

Interestingly, the Office of Federal Procurement Policy (OFPP) in OMB has proposed restructuring Attachment O of Circulars A-102 and A-110 in a manner similar to the restructuring we propose. Attachment O provides standards for procurement by recipients of Federal assistance. According to OFPP's proposal, if a recipient's procurement system meets minimum standards, Federal agencies' involvement would be limited to general oversight. If these standards were not met, agencies would have various options open to more thoroughly oversee recipient procurements. Some OMB officials believe that the restructuring of Attachment O is complementary to the act's grant and cooperative agreement categories.

While OMB is developing these distinctions, we believe it should also reconcile the primary organization of these two circulars to the act's basic framework. The act's legislative history indicates that:

> "The criteria established in sections 4, 5, and 6 of this bill are a beginning * * * in providing a framework of relationships for governmental guidance in assistance programs." (Emphasis added.)

The circulars' current orientation of providing assistance guidance initially by type of recipient does not mesh with the act's framework--type of legal instrument. In revising the guidance, OMB, however, might still want to preserve some variances by type of recipient. For example, within the guidance for either grant or cooperative agreement relationships, requirements for large recipients such as major cities might vary from those for very small ones like rural counties.

Modifications like these could facilitate achieving the act's purposes. First, a reduction in unnecessary administrative requirements might result because Federal officials would be selecting the optional grant or cooperative agreement requirements on the basis of a need for them in the particular relationship. For example, the city of Portsmouth, Virginia, was required to submit very detailed information to the Economic Development Administration (EDA) to justify its requests for reimbursement under an EDA discretionary grant. Although EDA staff originally wanted copies of actual checks, they agreed to accept schedules of each purchase order annotated with the check number and date. EDA had not explained to the city why such detail was required, such as notifying the city that its accounting systems were insufficient. If detailed records, such as these, could only be required under cooperative agreement options, and the Federal agency could not justify the use of a cooperative agreement, then the city would have had a clear avenue to dispute the requirement.

Second, the respective roles and responsibilities of the Federal Government and recipients would be clarified because the allowable Federal requirements and when they could be used would be more explicit.

Third, with operational differences developed, the Congress and the executive agencies could utilize the grant and cooperative agreement categories in their oversight and management of Federal programs. As shown in the legislative history, it was anticipated the act's categories would be useful for congressional oversight of assistance programs:

> "The broad statutory framework provided by this legislation will enable the Congress to exercise better oversight of agency attempts to bypass Congressional intent * * *."

For example, if a program that Congress intended to be operated primarily as a grant were to award numerous cooperative agreements, an oversight committee might question such awards. An analysis of the application of the act's categories could also be useful to agency officials. For example, a program that used a high proportion of cooperative agreements might require more staff than one using all grants. When allocating personnel among programs, agency officials could utilize data on the types of instruments used.

Finally, because the choice of either a grant or a cooperative agreement would have operational consequences, we believe Federal officials would have more incentive to select the proper instrument.

OMB Circulars A-102 and A-110 do not cover all Federal involvement with recipients. However, this other involvement is not subject to Government-wide guidance similar to the circulars and therefore is not ready to be structured as we propose for A-102 and A-110. Indeed, no one knows the full extent or diversity of agencies' involvement with recipients. One benefit of the interim approach we propose in chapter 2 for identifying cooperative agreements is that by studying the cooperative agreements thus identified, OMB may be able to learn more about the range of this involvement. OMB could then judge whether additional structuring of guidance around the grant and cooperative agreement relationships is appropriate. Perhaps such crosscutting guidance topics as civil rights, environmental protection, and energy conservation would lend themselves to restructuring too.

Although we believe that developing operational distinctions will enhance the achievement of the act's purposes, we recognize that developing the differences will not be easy. As in the determination of which rules should apply to assistance versus procurement, the development of guidance specific to grants and cooperative agreements will reflect Federal policy on the respective roles and responsibilities of the Government and recipients under the two assistance relationships. For example, some recipients feel that the involvement currently sanctioned by A-102 and A-110 is substantial. They would prefer to roll back the permissible level of involvement under grants rather than increase the level for cooperative agreements. Therefore, the development of new guidance specific to grants versus cooperative agreements should, as for assistance versus procurement, be made with due regard for the input of all potentially affected parties.

Establishing what the distinctions between these instruments should be and how they would be applied, will require an adequate data base on the different ways that Federal agencies presently interact with recipients and what their preferences, as well as recipients' preferences, would be for changing interactions. Because many officials believe that the type or level of Federal involvement should legitimately vary depending on the functional category of the program, e.g., construction programs, research programs, and social service delivery programs, the data base should be representative of the various categories of Federal assistance.

## CONCLUSIONS

The purposes of the Federal Grant and Cooperative Agreement Act cannot be fully achieved unless meaningful distinctions between the act's categories are developed. Operating distinctions between procurement and assistance appear to be eroding, and there are no standard operational differences between grants and cooperative agreements. Therefore, an effort must be undertaken to identify and promulgate consistent operational distinctions. Because establishing differences between the act's instruments will also establish Federal policy on the respective roles and responsibilities of the Federal Government and recipients, and because the act seeks to achieve uniformity in the use of contracts, grants, and cooperative agreements, we believe OMB is the best organization to lead the necessary Government-wide effort.

When determining the differences which should exist between procurement and assistance, we believe the act's criteria--the Federal purpose in the relationship--should be relied on in deciding which procedures are appropriate to each category. In deciding on operational distinctions between grants and cooperative agreements we believe further study should be made of how Federal agencies currently vary their interactions with recipients. Revising and reorganizing Circulars A-102 and A-110 to establish minimum requirements for any assistance award and optional requirements specifically available under grants and cooperative agreements seems to be a practical approach for establishing the needed distinctions between grants and cooperative agreements.

## RECOMMENDATION TO THE DIRECTOR, OMB

To improve the implementation of the Federal Grant and Cooperative Agreement Act, we recommend that the Director of OMB take the lead in establishing clear operational differences among contracts, grants, and cooperative agreements.

## AGENCY COMMENTS AND OUR EVALUATION

EPA and the Departments of the Interior and Justice agreed with our recommendation that OMB take the lead in establishing clear operational differences among contracts, grants, and cooperative agreements. OMB agreed to consider the recommendation during its current efforts to develop revised guidance implementing the act.

The Department of Energy said categorization of Circulars A-102 and A-110 would not help in differentiating between grants and cooperative agreements but might encourage agencies to adopt all of the more stringent requirements of cooperative agreements for fear of being thought irresponsible. We disagree. A clear distinction between the administrative requirements in these circulars by type of instrument will help Federal officials match their practices and procedures with the appropriate instrument. This will identify where substantial Federal involvement is occurring so that top executive officials and the Congress can approve or modify that involvement with recipients. Further, in that Federal officials would select cooperative agreement requirements on the basis of a need for them in a particular relationship we believe they will be less likely to become unnecessarily involved.

Energy was also concerned that we consider cooperative agreements to be the preferred instrument where additional requirements are needed for "high-risk" recipients. Energy believes the choice of grants or cooperative agreements is independent of the decision to include additional requirements for such recipients. Although we do not intend to suggest that all high-risk recipients should automatically receive cooperative agreements, additional requirements levied on them tend to indicate substantial involvement and are therefore directly related to the decision to use a grant or a cooperative agreement. Such requirements exist because the agency perceives a need to exercise more control, which is an expression of involvement, over a particular recipient. To the extent that the additional requirements exceed the norm for Federal involvement, a potential cooperative agreement relationship exists.

APPENDIX I

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

Mr. William J. Anderson
Director, General Government Division
United States General Accounting Office
Washington, D. C. 20548

Dear Mr. Anderson:

This is in response to your request of May 13, 1981, for comments on the draft GAO report entitled, "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act." The report presents a good review of an extremely complex subject and we are in general agreement with most of its contents. It will be of immediate use since we are revising the OMB guidance on implementing the Act issued in 1978.

The report recommends stronger OMB monitoring of agency efforts to implement the Act. The report concentrates on a single policy area. As we see it, however, the report documents symptoms of a larger problem. When one studies the ways that agencies have implemented the sixty-plus generally applicable assistance policies, the same basic picture tends to emerge. Viewed this way, the problem is one of improving the ways agencies manage all the requirements generally applicable to assistance programs and other Federal transactions, including the Federal Grant and Cooperative Agreement Act.

To address this larger management problem, we have in development and plan to issue shortly, a new OMB Circular on General Assistance Policies. This Circular will deal, in part, with the internal agency communication and coordination problems of assistance programs documented in the report. The revised guidance on implementing the Act will become an attachment to the new Circular. In addition, the Office of Federal Procurement Policy will communicate the portions of the revised guidance it concludes procurement officials should have.

I believe an additional point needs to be made for the record by OMB. The basic distinctions presented by the Act work and are used successfully by the agencies for most of their relationships. There are cases, however, as the report indicates, where the Act has led to confusion. On close examination, the Act turns out to contain a paradox.

The Act instructs agencies to use a procurement contract when the transaction provides something of direct benefit or use to the Government. One can reason that anything which helps an agency accomplish its mission is of benefit or use to the Government. Since virtually everything an agency does should be to accomplish its mission, it can be argued that all of its transfer activities should use procurement.

APPENDIX I

Conversely, the Act instructs agencies to use grants or cooperative agreements to "accomplish a public purpose of support or stimulation authorized by Federal statute." If an agency's mission is one of stimulation or support, and one reasons that all agency actions are in support of the mission, then one can conclude that grants or cooperative agreements are required for all actions. Thus, the Act can be seen as requiring the use of both procurement and assistance instruments for the same transaction.

Many of the examples of agency reasoning presented in the report show the effects of this paradox. Reasonable people in the agencies, trying to do the right thing, can and do reach different conclusions about which type of relationship to establish. Our concern for the agency actions described in the report is tempered by an appreciation of the magnitude of the problems presented to them by the Act.

The report includes eleven specific recommendations for OMB. Enclosed, are our responses to these useful suggestions. The fact that we differ on some of them is significant. For the past three and one half years, OMB and GAO staffs have cooperated closely in this field. They have shared information, ideas, and concepts. All along, it was intended that our two organizations should be able to cooperate and use a common data base without impairing their independence of judgement. I feel the experiment has worked, and I congratulate your staff members who contributed to its success.

Sincerely,

Harold I. Steinberg
Associate Director
for Management

Enclosure

OMB Response to GAO Recommendations
in the Draft Report
"Improvement Needed in the Implementation of the
Federal Grant and Cooperative Agreement Act"

The draft GAO report on the Federal Grant and Cooperative Agreement Act, sent to OMB for comment on May 13, 1981 contains eleven specific recommendations to the Director of OMB. Our responses to these recommendations follow:

Recommendations 1, 2, and 3: The first three recommendations are prefaced with:

> "To improve the selection of procurement contracts and assistance instruments, OMB should revise its guidance on the Federal Grant and Cooperative Agreement Act to."

GAO Recommendation 1:

"— more clearly define the terms "direct benefit and use" as they relate to the selection of contracts and "accomplishing a public purpose of support or stimulation" as it relates to assistance."

OMB Response: We agree. The revised implementing guidance will include an expanded discussion of these fundamental terms.

GAO Recommendation 2:

"— require Federal program officials to base instrument choices on the Federal purpose in the relationship established after (1) reviewing their authorizing legislation to determine their authority to procure or assist, and (2) reviewing each proposed transaction in light of the act's criteria."

OMB Response: We agree with one reservation. For the vast bulk of all assistance and procurement actions, it is not necessary to review each transaction. The revised guidance will call for such transaction level reviews only for those transactions that require it.

GAO Recommendation 3:

"— clearly state that section 7(a) of the act does not create new authority to make assistance awards independent of program legislation."

OMB Response: We agree, and the revised guidance will include such a statement.

Recommendations 4, 5, and 6 are prefaced with:

> "To help Federal officials identify potential awards where a cooperative agreement might be appropriate we also recommend that OMB revise its guidance specifically related to cooperative agreements. The revisions should:"

GAO Recommendation 4:

"-- define normal involvement, normal Federal stewardship, and substantial involvement. This could be accomplished by adopting our suggested interim program approach for assessing levels of involvement with program recipients."

OMB Response: We agree that the three terms need to be clarified, and will try to do so. The proposal for the interim program approach is a constructive suggestion which we will consider seriously. We are concerned, however, that the approach may require some agencies to change their interim decisions which could cause confusion and unwarranted uncertainty.

GAO Recommendation 5:

"-- recognize that highly prescriptive requirements prior to award limiting recipient discretion may constitute substantial involvement during performance whether or not they are coupled with close agency monitoring of, or operational involvement with, the recipient."

OMB Response: The Act differentiates between grants and cooperative agreements solely on the basis of substantial involvement anticipated during performance of the contemplated activity. While we understand the GAO intent, we do not agree that involvement during performance can be interpreted as including pre-award conditions that limit recipient discretion. We believe that involvement during performance of an activity must actually occur during the performance period.

GAO Recommendation 6:

"-- provide more detailed and complete illustrations of agency practices which can be considered as substantial involvement."

OMB Response: We will attempt to do this in the revised guidance. A more effective way, however, may be through inter-agency workshops and training sessions.

Recommendations 7, 8, 9, and 10 are prefaced with :

"To improve the administration and monitoring of the act, we recommend that the Director, OMB:"

GAO Recommendation 7:

"-- Direct Federal agencies to (1) develop administrative systems necessary to implement and monitor compliance with the act, (2) identify emerging problems so that revisions to policies and procedures can be considered, (3) provide adequate staff training and technical assistance on the act and OMB guidelines, and (4) develop systems of records on their operating experiences in implementing the act."

OMB Response: We believe that improvements can best be achieved by treating the Federal Grant and Cooperative Agreement Act as both a federal procurement policy and one of the generally applicable assistance requirements for which a broad assistance management policy circular is being developed. A draft of the circular policy was published in the Federal Register on November 7, 1980. A final version is expected to be issued in the next several months. This two-pronged approach that uses the existing procurement disciplines and strengthens assistance management on a broad scale gives promise of accomplishing more than concentration on just the Act.

GAO Recommendation 8:

"— Actively monitor the implementation by Federal agencies to assure that OMB policies and guidelines are carried out uniformly and in a timely manner."

OMB Response: This will be done as part of the larger effort on improving the management of generally applicable requirements. It may also be included as part of the Financial Priorities Program that agencies are now implementing under OMB guidance. But we believe that primary emphasis must be on helping the agencies manage themselves in accordance with the Act, rather than on monitoring what the agencies do.

GAO Recommendation 9:

"— Establish an effective, ongoing system to document and respond to problems identified during monitoring activities."

OMB Response: We believe the new policy for managing generally applicable requirements will contribute to this. Many of the problems can be resolved by the agencies themselves, once their internal management systems are developed to the point that they are routinely used.

GAO Recommendation 10:

"— Revise the OMB guidance to provide more insight into how agencies can avoid unnecessarily increasing Federal liability under cooperative agreements."

OMB Response: We agree and plan to do this.

GAO Recommendation 11:

To improve the implementation of the Federal Grant and Cooperative Agreement Act, we recommend that the Director of OMB take the lead in establishing clear operational differences among contracts, grants, and cooperative agreements.

OMB Response: This subject will be addressed in policy deliberations over the revised guidance that OMB is developing for the Act.

# United States Department of the Interior

OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20240

JUN 26 198

Henry Eschwege
Director
Community and Economic Development
Divison
U.S. General Accounting Office
Washington, D.C. 20548

Draft Report, "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act"

Dear Mr. Eschwege:

We have reviewed the subject draft report and agree with its findings and recommendations.

The report's basic finding is that the Congressional purpose in passing the Federal Grant and Cooperative Agreement Act, namely, to establish a systematic approach to distinguish contracts, grants and cooperative agreements, has been frustrated due to agencies misunderstanding key provisions of the Act. In order to improve understanding of the Act, the report makes several recommendations to the Director, Office of Management and Budget. These include:

1. Improving OMB guidance on how to distinguish procurement and assistance, and grants and cooperative agreements;

2. Increasing monitoring and administration of the Act by OMB and the agencies;

3. Establishing clear operational differences between contracts, grants and cooperative agreements.

Although we support the basic recommendations of the report, we have a couple of comments regarding the proposed interim procedure for determining "substantial involvement." While we agree that clearer guidance in determining what constitutes "substantial involvement" is needed, we wonder how useful it is to impose an interim system on the agencies, when, according to the report, revised OMB guidance is to be issued within the next several months. In addition, we wonder whether defining "normal involvement" in the context of individual programs will be any easier than defining "substantial involvement".

Thank you for the opportunity to comment.

Sincerely,

Deputy Assistant Secretary
Policy, Budget, and
Administration

APPENDIX III

**Department of Energy**
**Washington, D.C. 20585**

JUN 25 1981

Mr. J. Dexter Peach
Energy and Minerals Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Peach:

The Department of Energy appreciates the opportunity to review and comment on the General Accounting Office's draft report entitled "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act." The draft report contains a helpful discussion of the problems associated with implementation of P.L. 95-224 and makes generally useful recommendations for resolving them. DOE does, however, have reservations concerning some aspects of these recommendations.

The draft report expresses the opinion that highly prescriptive requirements imposed before an assistance award can in and of themselves, dictate use of a cooperative agreement. This differs from the existing Office of Management and Budget guidance which counsels that such requirements must be coupled with close agency monitoring or operational involvement during performance before a cooperative agreement is indicated. DOE finds the Office of Management and Budget's guidance to be more helpful. For example, an award made in response to an unsolicited proposal may need to be "highly prescriptive" in order to keep the project within limits which the agency may appropriately fund but differs in no other way from the typical grant as envisioned by P.L. 95-224.

The draft report suggests that an interim approach to further defining substantial involvement (prior to development of specific operational characteristics distinguishing grants and cooperative agreements) be based upon each agency's normative involvement characteristics either on an agency-wide basis or for individual programs and basing grant and cooperative agreement distinctions on how they are more or less involved with individual recipients. This approach is not entirely useful for two reasons. First, if the norms are developed by program rather than agency, it could lead to a given recipient receiving funding from two different programs in the same agency under different instruments while the federal involvement was essentially identical. Secondly, since it is an interim process, it could, for example, lead a program to shift from grants to cooperative agreements to grants again when final guidance was developed. In both cases the confusion generated among recipients and the resultant lack of confidence in the Federal Agency is difficult to accept.

APPENDIX III

The draft report also recommends increased Office of Management and Budget oversight of agency implementation of the Act as a way of improving compliance with the Act's provisions. DOE officials believe increased oversight will be of little value unless the guidance on implementing the Act is perfected. The problem is less one of bad faith than it is of genuine confusion and lack of operational experience. With better guidance, there will be less need for the Office of Management and Budget oversight.

DOE officials believe the draft report's proposal to categorize the provisions of the Office of Management and Budget's Circulars A-102 and A-110 by frequency of use or degree of detail will not assist in differentiating between instruments but might encourage Federal officials to adopt all of the more stringent requirements for cooperative agreements for fear of being thought irresponsible. DOE has not had any major difficulty in writing cooperative agreements that comply with the circulars. DOE notes that the draft report in its discussion related to this proposal implies that the Circulars' Exceptions for Certain Recipients provisions, which provide for increased requirements on what are commonly referred to as "high risk" recipients, be used to write in additional requirements generally on cooperative agreements. The further implication is that the General Accounting Office believes the cooperative agreement is the instrument of choice when dealing with a "high risk" recipient. DOE officials do not share this view, but believe the decision to use a grant or cooperative agreement is independent of the decision to include additional requirements in awards to high risk recipients. In addition, more attention needs to be focused on the fact that there is no guidance equivalent to OMB Circulars A-102 and A-110 for dealing with "for-profit organizations." Until such guidance is developed it can be expected that agencies will increasingly turn to Procurement Regulations for guidance in developing the rules for making assistance awards to for-profit organizations.

Again, DOE appreciates the opportunity to comment on this draft report and trusts that the General Accounting Office will consider these comments in preparing the final report.

Sincerely,

for William S. Heffelfinger
Assistant Secretary
Management and Administration

APPENDIX IV

U.S. Department of Transportation
Office of the Secretary of Transportation

Assistant Secretary for Administration

400 Seventh Street, S.W.
Washington, D.C. 20590

June 22, 1981

Mr. Henry Eschwege
Director, Community and Economic
Development Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Eschwege:

We have enclosed two copies of the Department of Transportation's (DOT) reply to the General Accounting Office (GAO) draft report, "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act," dated May 18, 1981.

DOT generally supports GAO'S findings with regard to implementation of the Act, but believes that it will be necessary to amend the statute itself so as to remove those impediments contained within the statute which thwart its basic purpose. We do not believe the recommendations made to OMB, although valid, can be accomplished without first revising the statute.

If we can further assist you, please let us know.

Sincerely,

Robert L. Fairman

Enclosures

DEPARTMENT OF TRANSPORTATION
STATEMENT ON GAO REPORT

I. TITLE: IMPROVEMENTS NEEDED IN THE IMPLEMENTATION OF THE FEDERAL GRANT AND COOPERATIVE AGREEMENT ACT

II. GAO FINDINGS AND RECOMMENDATIONS: The General Accounting Office (GAO) has reviewed Federal agency implementation of the Federal Grant and Cooperative Agreement Act (P.L. 95-224) to determine whether this implementation has been proper, and what Government-wide issues have resulted from implementation. GAO concluded that operating distinctions between procurement and assistance appear to be eroding, that there are no standard operational differences between grants and cooperative agreements, and that an effort must be undertaken to identify and promulgate consistent operational distinctions.

The GAO recommends that the Office of Management and Budget (OMB) revise its guidance on the Federal Grant and Cooperative Agreement Act to

--More clearly define the terms "direct benefit and use" as they relate to the selections of cutbacks, and "accomplishing a public purpose of support or stimulation" as it relates to assistance.

--Require Federal program officials to base instrument choices on the Federal purpose in the relationship established after (1) reviewing their authorizing legislation to determine their authority to procure or assist, and (2) reviewing each proposed transaction in light of the Act's criteria.

--Clearly state that section 7(a) of the Act does not create new authority to make assistance awards independent of program legislation.

--Revise its guidance specifically related to cooperative agreements. The revisions should

--Define normal involvement, normal Federal stewardship, and substantial involvement.

--Recognize that highly prescriptive requirements prior to award limiting recipient discretion may constitute substantial involvement during performance whether or not they are coupled with close agency monitoring of, or operational involvement with, the recipient.

--Provide more detailed and complete illustrations of agency practices which can be considered as substantial involvement.

--Direct Federal agencies to (1) develop administrative systems necessary to implement and monitor compliance with the Act, (2) identify emerging problems so that revisions to policies and procedures can be considered, (3) provide adequate staff training and technical assistance on the Act and OMB guidelines, and (4)

APPENDIX IV

develop systems of records on their operating experiences in implementing the Act.

--Actively monitor the implementation by Federal agencies to assure that OMB policies and guidelines are carried out uniformly and in a timely manner.

--Establish an effective, ongoing system to document and respond to problems identified during monitoring activities.

--Revise the OMB guidance to provide more insight into how agencies can avoid unnecessarily increasing Federal liability under cooperative agreements.

III. DOT COMMENTS ON FINDINGS AND RECOMMENDATIONS:

GENERAL:

The Department of Transportation generally supports GAO's findings with regard to implementation of the Act, but believes that it will be necessary to amend the statute itself so as to remove those impediments contained within the statute which thwart its basic purpose. We do not believe the recommendations made to OMB, although valid, can be accomplished without first revising the statute.

SPECIFIC:

CHAPTER 2. INCORRECT INSTRUMENTS CAN BE CHOSEN BECAUSE GUIDANCE IS VAGUE

Clearer Terms and Procedures Needed to Distinguish Between Procurement and Assistance

The Department of Transportation agrees that there is a need for clearer terms and procedures as cited by GAO, but believes that the starting point for any such action should be the statute itself. The term "Direct Benefit and Use of the Government" contained in Sec. 4(1) has been utilized to thwart the basic intent of the statute. The Federal Grant and Cooperative Agreement Act (P.L. 95-224) was primarily enacted to establish clear distinctions between procurement and assistance, however, language such as mentioned above only contributes to the further misuse of assistance instruments in situations which are clearly procurement. We in the Department of Transportation were able to deal with problems in the basic statute by employing provisions such as section 4(2) by requiring the use of a procurement instrument whenever the Department is purchasing property or services regardless of whether the intended beneficiary is the Department itself or a third party. Furthermore, we require that the focus be on the immediate transaction between the Department and the party with which we are entering into the transaction. If we are buying from that party, procurement is required, if we are primarily assisting that party, an appropriate assistance instrument is required.

Section 4(2), of the Act provides that a procurement contract shall be used whenever an executive agency determines in a specific instance that the use of a type of procurement contract is appropriate. If it were not for this provision, we do not believe we would be in conformance with the Direct Benefit and Use requirement contained in section 4(1) of the statute if we required procurement in situations other than when the Department is the direct recipient or user under the agreement. In the draft report, GAO contends that agencies have misunderstood section 4(1) particularly with regard to intermediaries. We agree that transactions requiring intermediaries should be in the procurement mode, but we do not believe that section 4(1) can be the basis for such action given the "direct use and benefit" language currently contained therein. In fact, the legislative history for section 4(2) indicates that it is that section and not section 4(1) that was enacted to accommodate situations where it is desired to utilize an intermediary through the use of the procurement process. The problem is that section 4(2) is permissive, and thus perpetuates inconsistency of treatment in situations involving intermediaries.

We recommend that the report contain a recommendation to the Congress to delete the term "Direct Benefit and Use of the Federal Government" from the statute so that it will be mandatory to utilize the procurements process whenever the Federal Government is purchasing property or services regardless of whether for itself or third persons through an intermediary.

CHAPTER 3. STRONGER OMB AND AGENCY MANAGEMENT EFFORTS NEEDED TO IMPLEMENT THE ACT.

On August 23, 1979, the Department of Transportation issued DOT 4000.8, Use of Contracts, Grants and Cooperative Agreements. The Order followed OMB guidance establishing criteria for distinguishing between procurement and assistance. However, there are very few programs within the Department that are involved in other than assistance activities. The one program that is involved in procurement and assistance activities has been monitored very closely to make sure that the proper instruments are being utilized. With regard to our assistance programs, we do not perceive any change in the substance of our agreements and after close analysis concluded that the majority of projects would be properly categorized as cooperative agreements. It is important to note, however, that we see this as nothing but a relabeling exercise with business as usual as far as the administration of these projects is concerned. Perhaps there is a need for stronger management efforts to implement the Act with regard to other Federal programs, but we see no such need in this Department.

Problems with section 7(a)

We fully agree with GAO on this point and have utilized section 7(a) as a mechanism authority only. It does not impact on the program substance which originates in authorizing legislation. Section 7(a) only provides flexibility in selecting the instrument to be used in carrying out that activity. If an assistance instrument is selected, there must be authority to provide assistance in the authorizing legislation. Section 7(a) does not create the authority to provide assistance.

APPENDIX V

CHAPTER 4. NEED TO DEVELOP DIFFERENCES IN OPERATING PROCEDURES FOR GRANTS, COOPERATIVE AGREEMENTS, AND CONTRACTS

Before we attempt to develop criteria clearly defining substantial involvement, and before we attempt to distinguish grants from cooperative agreements, we should first decide the merit to such exercises. What is the need? Is it merely an unnecessary bureaucratic exercise? We see absolutely no reason for the cooperative agreement category. It merely muddies the water and creates further opportunity for program officials to avoid the Federal Procurement Regulations. If there were two general categories, Procurement and Assistance, with subcategories under each (as there presently is under Procurement) to accommodate the peculiarities of particular transactions, the original purpose of the statute could be achieved in a relatively simple manner. This can only be achieved through statutory revision, and we recommend that the GAO consider this position and make appropriate recommendations to the Congress.



"BEST COPY AVAILABLE"

APPENDIX V

U.S. Department of Justice

JUN 18 1981

*Washington, D.C. 20530*

Mr. William J. Anderson
Director
General Government Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Anderson:

This letter is in response to your request to the Attorney General for the comments of the Department of Justice (Department) on your draft report entitled "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act."

The Department generally concurs with the findings and recommendations of the draft report. In particular, the Department agrees that the Office of Management and Budget (OMB) should establish clear operational differences among grants, contracts, and cooperative agreements, and develop additional guidance on how to select the proper instrument based on various agencies' experience to date.

As the report indicates, the Department's National Institute of Corrections (NIC), like other Federal agencies, has found considerable ambiguity to exist regarding clear operational differences between contracts, grants and cooperative agreements and has experienced difficulty in determining when to use cooperative agreements or contracts to reflect different levels of Federal involvement in assistance relationships or procurement situations. However, the Department agrees with the General Accounting Office's (GAO) observation that Congress did include a specific authorization in NIC's legislation giving NIC authority, in procurement situations:

> "to enter into contracts with public or private agencies, organizations, or individuals, for the performance of any of the functions of the Institute * * * ." (18 U.S.C. 4352(a)(13).) (Emphasis added.)

In view of the total range of issues raised by GAO, NIC has reviewed its assistance and procurement efforts to more closely distinguish between the two. Where a clear distinction between the two appears ambiguous, the guidance provided by the subject GAO report will be employed pending the dissemination of more detailed guidance by OMB.

Although not included in GAO's study, the Department's Office of Justice Assistance, Research and Statistics (OJARS) has had considerable experience with grants, contracts, and cooperative agreements and has devoted substantial effort to the interpretation and implementation of the Federal Grant and Cooperative Agreement Act. Based on its experiences, OJARS generally agrees with the findings and recommendations of the report, but differs with GAO in its interpretation of some of the issues raised in the report.

APPENDIX V

On page 31, GAO states that "Agencies also have not established effective mechanisms to insure that agency officials use the guidelines or apply them properly." OJARS has not experienced such problems and, in fact, has been effective in implementing the alternate funding approaches in an appropriate manner. Unlike many of the agencies surveyed by GAO, OJARS has an agency-wide instruction on this subject, although it requires updating to reflect experience to date.

GAO's main point in Chapter 2 is that agencies have been using improper criteria or questionable interpretations of vague OMB guidance in making determinations of the appropriate instrument to use. We agree that where a procurement relationship is clearly established, a contract is required as pointed out in the example on page 9. We also agree that agencies keying on the "direct benefit" language of the Act can lead to the inappropriate use of assistance instruments where a contract is indicated as in the example on pp. 9-10. However, we believe that the inflexible approach (interpretation) set forth by GAO in the last paragraph of page 10 of the draft report does not reflect Congressional intent.

GAO takes the position that the proper interpretation of the Federal Grant and Cooperative Agreement Act of 1977 requires, in situations where agencies use "intermediaries" to provide assistance to eligible beneficiaries of Federal financial assistance, that the relationship between the Federal Government and the intermediary be reflected in a contract rather than a grant. It is our opinion that this GAO interpretation conflicts with the plain language of the Act.

Section 4 of the Act requires the use of contracts:

> ". . . whenever the principal purpose of the instrument is the acquisition, by purchase, lease, or barter of property or services for the direct benefit or use of the Federal Government." (Emphasis added.)

Section 5 and Section 6 of the Act require, in pertinent part, that assistance instruments (grants, cooperative agreements) be used "whenever the principal purpose of the relationship [between the Federal Government and the recipient] is the transfer of money, property, services, or anything of value to the State or local government or other recipient in order to accomplish a public purpose of support or stimulation authorized by Federal statute, rather than acquisition, by purchase, lease or barter, of property or services for the direct benefit or use of the Federal Government." (Emphasis added.)

GAO states in their interpretation that the choice of instrument for an intermediary relationship must depend solely on the Federal purpose in establishing the relationship with the intermediary because it (the intermediary) is the direct recipient of the Federal award. GAO concludes that Federal agencies have given inappropriate emphasis to the term "direct benefit" used in Section 4 of the Act with the result that such agencies have inappropriately tended to look at the extent of benefit received by beneficiaries of the Federal assistance who are not parties to the instrument.

In situations where the primary beneficiaries of Federal assistance are nonparty beneficiaries, i.e., not the intermediary, many Federal agencies have interpreted the Act and regulations to permit the use of an assistance instrument rather than a contract. According to GAO's interpretation, this agency interpretation is incorrect. GAO asserts that a contract relationship should be established.

Our view is that GAO's interpretation is inconsistent with the plain language of the above-cited statutory sections. Section 5 and Section 6 state that an assistance instrument must be used whenever the principal purpose of the relationship is to accomplish a public purpose of support or stimulation. It does not indicate who is to be supported or stimulated. Had Congress intended to require that the support or stimulation be only of the immediate party to the instrument, then it could easily have so stated.

Section 4 of the Act states, and Sections 5 and 6 of the Act reiterate, that a contract will be used whenever the principal purpose of the relationship is to provide property or services for the direct benefit or use of the Federal Government. GAO's interpretation would give the word "direct" no meaning. We believe that when the relatively restrictive term "direct benefit" is compared with the relatively broad term of "support or stimulation," it is clear that the latter was intended to be more inclusive than the former. Thus, the plain language of the statute would support, in may intermediary situations, the use of an assistance instrument rather than a contract. A contract is the only appropriate instrument only when the principal purpose of the relationship is to obtain a product or service for the direct benefit or use of the Federal Government. An assistance instrument should be used in all other situations where the principal purpose of the instrument is support or stimulation of any authorized recipient. This interpretation is fully consistent with the statute's plain language.

There is an important qualifier that must be added to this discussion: the intermediary must be a statutorily eligible recipient of the assistance. This qualifier requires that the intermediary be expressly authorized under the agency's enabling statute to receive the assistance. This condition is stipulated by the definition of the term "other recipient" in the Act. "Other recipient" is defined as "any person or recipient" other than a State or local government who is authorized to receive Federal assistance or procurement contracts . . . ." (Emphasis added.) Many grant statutes have limitations on the types of recipients eligible to receive funding. Thus, if the intermediary is not itself authorized to receive assistance under the statute, then a contract would be required. This qualifier is in addition to the qualifier noted by GAO--that the statute must, in the first instance, authorize the agency to "stimulate and support" before any assistance instrument can be used (draft report, pp. 14-20).

With regard to other matters covered in Chapter 2, we disagree with GAO's opinion that prescriptive requirements limiting a recipient's management discretion prior to award or during performance are themselves indicative of an agency's substantial involvement. We think the current OMB guidance better reflects the concept of substantial involvement.

APPENDIX V

In conclusion, while we are in agreement with most aspects of the report, we are left with the distinct impression that it is overly contract oriented to the detriment of the type of agency flexibility that was intended by Congress under the Federal Grant and Cooperative Agreement Act. GAO fails to recognize the additional dimensions of flexibility, speed, and recipient control and discretion that are by-products of properly employed assistance instruments. These advantages over contracts, in appropriate assistance situations, should not be minimized.

We appreciate the opportunity to comment on the draft report. Should you desire any additional information, please feel free to contact me.

Sincerely,

for Kevin D. Rooney
Assistant Attorney General
for Administration

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410

June 18, 1981

OFFICE OF THE ASSISTANT SECRETARY
FOR ADMINISTRATION

IN REPLY REFER TO:

Mr. Henry Eschwege
Director, Community and
Economic Development Division
General Accounting Office
Washington, D.C. 20548

Dear Mr. Eschwege:

Your letter of May 18, 1981 requested the Department's comments concerning the draft GAO report entitled "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act."

In general, we find the draft report to be well written, fair and constructive. Although the report takes issue with some of the interpretations of the proper legal instrument made by agency officials, it points out that the legislation "is not a model of clarity" and that "it is not too surprising that Federal agencies interpret and apply the criteria in various ways and continue to use grants and cooperative agreements in what appears to be procurement situations."

The Department's principal concern with the draft report relates to your Office's interpretation regarding the Act's mandate to use a procurement contract as the legal instrument "whenever the principal purpose of the instrument is the acquisition, by purchase, lease or barter, of property or services for the direct benefit or use of the Federal Government." This mandate is contrasted with the Act's requirement to use an assistance instrument when "the principal purpose of the relationship is the transfer of money, property, services, or anything of value to the State or local Government or other recipient in order to accomplish a public purpose of support or stimulation authorized by Federal statute."

The GAO interpretation of the use of intermediaries (recipients of Federal awards who deliver authorized assistance to third parties) would authorize assistance awards to such entities only if the agency is authorized to directly assist those entities. As indicated on page 10 of the draft report:

> Our interpretation of the Act is that the choice of instrument for an intermediary relationship depends solely on the Federal purpose in the relationship with the intermediary since it is the recipient of the Federal award.

APPENDIX VI

The fact that the product or service produced by the intermediary pursuant to the Federal award may flow to and thus benefit another party is irrelevant. What is important is whether the Federal Government's purpose is to acquire the intermediary's services, which happen to take the form of producing the product or carrying out the service that is then delivered to the assistance recipient, or if the Government's purpose is to assist the intermediary to do the same thing. In other words, where the recipient of an award is not an organization that the Federal agency is authorized to assist, but is merely being used to provide a service to another entity which is eligible for assistance, the proper instrument is a contract.

We would contend that the words "to accomplish a public purpose of support or stimulation authorized by Federal statute" do not imply that only recipients authorized by statute to be supported or stimulated can be direct recipients of Federal assistance awards. In our view, the major factor in distinguishing between assistance and acquisition relationships when intermediaries are involved is whether or not the Government becomes the intermediary in conveying the assistance. If a recipient's products or services are delivered to the Government which uses them to convey assistance to the third party, that initial relationship should be established in the form of a procurement contract since the recipient's products or services are for the Government's "direct benefit or use." If however the recipient delivers products or services to a third party which is authorized by statute to be supported, the Government is not receiving the "direct benefit or use" of those products or services and therefore an assistance instrument should be used.

The fact that both interpretations can be accommodated under the existing legislation and OMB guidance is indicative of the need for refinements in that guidance. We would only stress that such refinement need not entail the wholesale elimination of assistance awards to recipients not specifically authorized to receive them. Improved guidance or examples concerning the "direct benefit or use" test would be just as productive and would appear to yield more uniformity of interpretation and application.

The draft report indicates that OMB will soon be issuing new guidance concerning the Act. It is strongly recommended that your Office defer issuance of the final report until an assessment of that guidance can be made and the remaining problems addressed.

We appreciate the opportunity to review the draft report.

Sincerely,

Albert J. Kliman
Acting Deputy Assistant Secretary

UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

30 JUN 1981

Mr. Henry Eschwege
Director
Community and Economic Development Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Eschwege:

The Environmental Protection Agency (EPA) has reviewed the General Accounting Office (GAO) draft report entitled "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act."

We believe this report constitutes a reasonable summary and assessment of agencies' experience in implementing the Federal Grant and Cooperative Agreement Act (FGCAA). We appreciate the thorough job GAO has done in researching some very complicated questions related to implementing FGCAA and in suggesting interpretations or other approaches which can help the Agency do a better job. There are, however, a few points which we believe should be clarified in the final report.

FGCAA required Federal agencies to make significant changes in policies and procedures for awarding assistance and procurement contracts. The difficulties in implementing these changes were compounded by the ambiguous language of the Act. The draft report confirms that "(t)he act's terms and legislative history and OMB's guidance have fostered inconsistent interpretations" (page 8, paragraph 1) and "(t)he act is not a model of clarity" (page 8, paragraph 4). On page 7, the report states that during GAO's review of agency actions in researching this and other reports, GAO found "several actual or proposed assistance awards which we believe should have been procurement contracts." Considering the thousands of awards made since passage of this Act, the record seems to be a good one.

Attached are specific comments relating to the draft report which we feel should be considered. In addition, two pages from the draft report requiring technical/typographical corrections are attached. (See GAO note.)

APPENDIX VII

We appreciate the opportunity to comment on the draft report prior to its issuance to Congress.

Sincerely yours,

Roy N. Gamse
Acting Assistant Administrator
for Planning and Management

GAO Note: We did not include these two pages in the final report.

APPENDIX VII

## Specific Comments

### CHAPTER 1

We particularly agree with the paraphrasing of the "public purpose of support or stimulation" language of the Act on page 1, paragraph 2, item (2), to indicate that assistance agreements are used "to support or stimulate activities" (emphasis added). However, on page 11, paragraph 2, the report indicates that assistance agreements may be used only when an agency has statutory authority "to support or stimulate someone else" (emphasis added). This is an important shift in terminology which may not have been intentional, although we believe it is incorrect. This position remains consistent with our support for GAO's interpretations of section 4(1) of the Act, as stated in Chapter 2.

We are concerned about the sweeping generalizations and statistics based on GAO's questionnaire. For example, one EPA official was called twice by different interviewers, who we believe were administering the same questionnaire. The interviewee is convinced the interviewers had no practical knowledge of grant assistance or how different agencies operate. The interviewers asked questions which were irrelevant to the interviewee's role and insisted that he answer, even though the answer may not have been pertinent to the employee's responsibilities or the Agency. While we hesitate to generalize from one experience, we are concerned that this experience may have been more widespread and rendered less-than-valid data.

### CHAPTER 2

We agree with the GAO interpretation of the "direct benefit" language in Section 4(1) of the Act.

We agree with the GAO interpretation of Section 7(a) of the Act. The Agency's Office of General Counsel believes their interpretation of the Act and their guidance to EPA officials in implementing the Act has been consistent with the opinion of the Acting General Counsel of the Department of Energy, as quoted in the draft report, page 18. Nevertheless, GAO cites EPA as an agency which does not share the opinion of the Acting General Counsel of the Department of Energy. We believe that this is a misrepresentation of EPA's position. To support this characterization, GAO cites one program in which an error was made while implementing the Act in 1979.

APPENDIX VII

This is an aberration of EPA's implementation of the Act. In the same paragraph, GAO points out that cooperative agreements based on assistance authority in the program legislation could have been used in the particular example. If this is GAO's interpretation, then EPA was not in violation of FGCAA.

We request clarification of GAO's suggested interim agency or program approach to defining normal or substantial involvement (page 26 ff.). In the second paragraph on page 27, the draft report states "the fact that a recipient is treated differently, that is, subjected to more controls and collaboration and less discretion than the normal recipient for a given program" (emphasis added), would suggest that the Federal agency is substantially involved and a cooperative agreement may be appropriate." This would mean GAO considers the normal instrument in every program (in this second test) to be a grant. However, on page 28, paragraph 2, the draft report indicates that agencies should "identify what is normal involvement for their programs and base their grant and cooperative agreement distinctions on how they are more or less involved than normal with individual recipients" (emphasis added.) This suggests that an agency could define the norm for each program as a grant or a cooperative agreement, with variations specifically justified. We agree with the latter statement. As now written, the recommendation beginning "define normal involvement, ..." on page 30 does not clearly reflect the discussion on pages 28-29; it should be revised to do so. Further, we suggest that this approach may be valid as a permanent, rather than an interim one.

We believe it would be helpful for agencies' continued implementation of the Act if GAO would express their opinion of the proper interpretation of section 4(2) of the Act.

CHAPTER 4

We support the main recommendation that OMB should revise its Circulars to establish clear operational differences for grants and cooperative agreements. We also agree that the report's suggested approach (minimum, optional, and maximum requirements), on page 49, is a good starting place for a redrafting effort. This would be consonant with our view that each agency is in the best position to determine the level of operational activities appropriate to its programs. The current distinctions between types of recipients (State and local governments in A-102 and institutions of higher education, hospitals, and other non-profit organizations in A-110) can be maintained with the legal instrument distinctions within each Circular. Alternatively, OMB could structure the Circulars (or a single Circular, preferably) by type of instrument with recipient distinctions within them.

ACTION
WASHINGTON D.C. 20525

OFFICE OF
THE DIRECTOR

Mr. Gregory Ahart, Director
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Ahart:

Thank you for allowing ACTION the opportunity to review the proposed report entitled "Improvements needed in the Implementation of the Federal Grant and Cooperative Agreement Act."

Due to the vagueness of existing guidance and the lack of specific operating procedures, progress in achieving the Act's objectives has been limited. In the face of incomplete or nonexistent operational guidance, agencies have frequently resorted to inappropriate procurement practices. For these reasons GAO should be applauded for its initiative in taking on this effort to improve the Act.

I have asked my staff to review the draft report and offer the following comments:

1) The suggested approach to further defining substantial involvement described on page 26 may be counter-productive. Requiring individual agencies or programs to develop characteristics for distinguishing between grants and cooperative agreements, even on an interim basis until OMB develops better guidelines, could result in more firmly entrenched differences among agency interpretations of the Act's requirements. This, in turn, would place additional and conflicting reporting burden on recipients engaged in similar activities under grants from some agencies and cooperative agreements from others.

This suggestion appears to conflict with the conclusion on page 29, that "[b]etter definition of... substantial involvement [is] needed to promote more consistent agency decisions.

2) The draft's argument for restrictive interpretation of Section 7(a) is not persuasive. (Pages 14-16 and 30.) The legislative history cited does not clearly indicate that Congress did not intend an expansion of grant authority. The cited legislative history explains that,

> [i]f an agency is presently authorized only to enter into <u>either</u> contracts, grants, cooperative agreements, <u>or</u> other arrangements, this authorization enables that agency to enter into <u>any or all three</u> types of agreements... (emphasis added).

In the draft this language is interpreted to mean that "Section 7(a) of the act does not create new authority to make assistance awards independent of program legislation," and suggests that OMB revise its guidance to "clearly state" this interpretation.

Another reasonable interpretation of the legislative history is that an agency previously authorized by its organic legislation to enter into only contracts may now enter into grants and cooperative agreements as well, unless its legislation specifically prohibited such assistance activities. If there is disagreement on Congress' intent, clarification should come from Congress, not OMB.

3) The first recommendation to the Director of OMB on page 43 would increase the regulatory and paperwork burdens on Federal agencies. This recommendation calls for the development of new "administrative systems" for implementing and monitoring compliance with the Act, and new "systems of records on [agencies'] operating experiences in implementing the act." Similarly, the suggestion on page 51 that an "agency might want to obtain financial reports on a monthly basis" for new recipients of assistance would increase the reporting burdens already imposed on grantees.

4) The discussion on termination of assistance for Federal convenience" on page 47 fails to take into account statutory requirements such as Section 412 of the Domestic Volunteer Service Act of 1973, as amended, P.L. 93-113. That section authorizes the Director of ACTION to terminate grant assistance "whenever he determines there is a material failure to comply with the applicable terms and conditions" of a grant. It also sets forth certain specified due process requirements to be followed in grant termination procedures.

If you have any questions or with further information on these comments, please let me know.

Sincerely,

Thomas W. Pauken

Thomas W. Pauken
Director

APPENDIX IX

DEPARTMENT OF HEALTH & HUMAN SERVICES

Office of Inspector General

Washington, D.C. 20201

24 JUN 1981

Mr. Gregory J. Ahart
Director, Human Resources Division
United States General Accounting Office
Washington, D.C. 20548

Dear Mr. Ahart:

Thank you for the opportunity to review and comment on the draft report entitled, "Improvements Needed in the Implementation of the Federal Grant and Cooperative Agreement Act." It is a very thorough and objective anaiysis of the Act. The Office of Inspector General will continue to evaluate compliance by Departmental components with the spirit and intent of the Act as part of our ongoing audit effort. Also, copies of the final version of this report will be furnished our audit staffs upon its release to illustrate the need for this continual monitoring. Inasmuch as there are no specific problems or recommendations regarding this Department, we have no other comments.

Sincerely,

Richard P. Kusserow

Richard P. Kusserow
Inspector General

(017630)



* U. S. GOVERNMENT PRINTING OFFICE : 1981 341-843/767